104

TRADE ISSUES REGARDING CHILE AND OTHER LATIN AMERICAN COUNTRIES IN LIGHT OF THE NAFTA EXPERIENCE

Y 4. IN 8/16: T 67/4

Trade Issues Regarding Chile and Ot...

HEARING

BEFORE THE

SUBCOMMITTEES ON
INTERNATIONAL ECONOMIC POLICY AND TRADE

AND

THE WESTERN HEMISPHERE

COMMITTEE ON
INTERNATIONAL RELATIONS
HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTH CONGRESS

FIRST SESSION

OCTOBER 25, 1995

Printed for the use of the Committee on International Relations

DEPOSITORY

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TRADE ISSUES REGARDING CHILE AND OTHER LATIN AMERICAN COUNTRIES IN LIGHT OF THE NAFTA EXPERIENCE

WEDNESDAY, OCTOBER 25, 1995

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON INTERNATIONAL ECONOMIC POLICY AND TRADE,
SUBCOMMITTEE ON THE WESTERN HEMISPHERE,
COMMITTEE ON INTERNATIONAL RELATIONS,
Washington, DC.

The subcommittees met, pursuant to call, at 10:07 a.m. in room 2172, Rayburn House Office Building, Washington, DC, Hon. Dan Burton and Toby Roth [chairmen of the subcommittees] presiding.

Mr. BURTON [PRESIDING]. The hearing will come to order. All members of the two subcommittees involved will not be here at the beginning of this hearing because we have a Republican conference going on at the same time. Other members will be drifting in as we get started.

I would like to welcome all of today's witnesses who are joining us here. I would also like to thank my distinguished colleague and chairman of the subcommittee on International Economic Policy and Trade, Toby Roth. He will be here in a few moments.

We are jointly sponsoring today's hearing on "Trade Issues Regarding Chile and Other Latin American Countries in Light of the NAFTA Experience." The House Ways and Means Committee on International Trade has already held hearings on this subject. I believe it is also important for our subcommittees to exercise our jurisdiction over these important trade issues.

In December, 1994, at the Summit of the Americas in Miami, the three North American Free Trade Agreement partners, the United States, Canada and Mexico, invited Chile to enter into negotiations to accede to NAFTA.

Furthermore, the Clinton administration has expressed its view that Chile accession's to NAFTA is a first step in establishing a Free Trade Area of the Americas, FTAA, by the year 2005; a goal that was established by those nations participating at the summit in Miami.

As Congress continues to evaluate Chile's potential accession to NAFTA, more people are calling attention to the problems of the U.S.-Mexico economic relationship since the passage of NAFTA and asking whether the United States can expect to encounter any similar problems with Chile if it joins the agreement.

It is my hope that this hearing will provide Members of Congress a chance to examine NAFTA's real impact on the United States since its implementation in January 1994. I am especially interested to hear from our witnesses as to whether the United States has lost more jobs than it has gained as a result of NAFTA; particularly in the wake of Mexico's peso devaluation.

This hearing should also give members a chance to compare the economic and political policies of both Chile and Mexico. This year, old tensions regarding past human rights abuses committed under the dictatorship of General Pinochet have resurfaced between the Chilean government, led by President Eduardo Frei, and the military still dominated by General Pinochet.

Many opponents of NAFTA expansion have argued that future political instability in Chile could negatively impact Chile's economy the same way as the Chiapas uprising damaged Mexico's economy.

While proponents of NAFTA expansion have dismissed this possibility, emphasizing the strength of Chile's economy and its historical support for democracy, today's hearing should provide our members the opportunity to explore this matter further.

Let me state for the record that I was opposed to NAFTA because I did not believe that tariff barriers between the United States and Mexico were being reduced equally. In addition, I prefer to resolve trade disputes bilaterally and not through multilateral dispute panels as were developed under NAFTA.

Despite my opposition to NAFTA, I do believe there are sound opportunities for the United States to open foreign markets to more U.S. products. I also believe that the United States must pursue these opportunities aggressively.

Within the Western Hemisphere, there is probably no better potential trade partner than Chile. As chairman of the Western Hemisphere Subcommittee, I am fully aware that if we do not promote free trade in Latin America, that this region will forge ahead without us, perhaps in partnership with the European Union.

Just this January, the Southern Cone common market, whose members include Argentina, Brazil, Paraguay and Uruguay, became a customs union. Chile is now negotiating associate status with MERCOSUR and holding discussions with the European Union.

Therefore, I am hopeful that Congress and the Administration can quickly resolve such outstanding issues as fast track and hammer out a session for Chile that addresses these concerns held by many of NAFTA's opponents.

Today we will receive testimony from three panels. The first panel includes four distinguished Members of the U.S. Congress. They are The Honorable Marcy Kaptur, Representative from Ohio; The Honorable Jim Kolbe, Representative from Arizona; The Honorable Jennifer Dunn, Representative from Washington; and The Honorable Duncan Hunter, Representative from California.

The second panel consists of three witnesses from the Administration. They are The Honorable Ira Shapiro, Special Negotiator for Japan and Canada in the Office of the U.S. Trade Representative; The Honorable Alexander Watson, Assistant Secretary for Inter-American Affairs with the Department of State; and William

Barreda, Deputy Assistant Secretary for Trade and Investment Policy at the Department of Treasury.

The last panel consists of two private sector witnesses: Dr. Sidney Weintraub, who holds the William B. Simon Chair in Political Economics at the Center for Strategic and International Studies; and Kevin Kearns, who is president of the U.S. Business and Industrial Council.

Once again, I welcome all of you to today's hearing. Representative Roth, my co-chair for this meeting, do you have an opening statement?

Mr. ROTH. Thank you, Mr. Chairman. I appreciate you having this meeting. I see we have some of our colleagues here this morning, and I do not want to hold them up so I will just introduce my opening statement into the record.

I will just say that I am delighted to have our four—three here—colleagues. I know how interested they are in trade, and 80 percent of all of our gross national product increase comes from the area of trade. Our best jobs are dedicated to those portions where we have a large overseas trade.

I think this is a very important hearing, Mr. Chairman. I am just delighted to be a part of it and listen to our colleagues, whose opinions we will take very seriously.

Mr. BURTON. Thank you, Mr. Chairman.

We will start and alternate between proponents and opponents of NAFTA. Why do we not start with Mr. Kolbe?

We will try to keep our remarks to 5 minutes so we can have time for questions.

STATEMENT OF THE HONORABLE JIM KOLBE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ARIZONA

Mr. KOLBE. Thank you, Mr. Chairman. I appreciate this opportunity to testify. I want to commend both Chairman Roth and Chairman Burton for holding this important hearing.

Given Mexico's current, though I think temporary, economic problems, it is certainly appropriate that we take stock of how NAFTA is working before we take the next step toward the clear mandate of the Summit of the Americas meeting last December, which is hemispheric free trade.

Today I want to tell you why I think NAFTA is working as it was intended to do and why it is critical to the economic future of the United States to continue to pursue hemispheric free trade.

I will make my spoken remarks fairly brief and ask that my whole statement be included in the record.

It has been nearly 2 years since Congress passed NAFTA and since it went into effect. However, we should remember that trade agreements are a long-term proposition. There are going to be short-term fluctuations which will have both positive and negative effects on U.S. interests. We would do well to remember that NAFTA is a foundation for North American trade phased in over 15 years.

Under the terms of the agreement, many of its most critical provisions have not even begun to be implemented. I think that is an important point. Still, it can be said that NAFTA is working.

During good times it spurs economic growth. It creates jobs on both sides of the border. When an economic upheaval occurs such as the peso devaluation this last winter, it cushions the impact domestically, limiting U.S. job losses and preserving jobs. NAFTA is a safety net for more than 700,000 U.S. workers whose jobs are supported by U.S. exports to Mexico.

NAFTA had a very good first year. Prior to devaluation of the peso last December, $20 billion of new trade took place between the United States and Mexico. One-fifth of all U.S.-Mexico bilateral trade was new trade generated in the first year of NAFTA. Although exports are down by 9.6 percent this year, they are still 7 percent higher than pre-NAFTA levels.

The best test of any agreement, I think, is how it works when times are bad. What NAFTA did was lock in Mexico's trade and economic reforms. NAFTA prevented Mexico from resorting to the standard solution of developing countries in crisis; that is, imposing import barriers, restricting capital movements, limiting economic activity.

In fact, this is precisely what was Mexico's response to the last financial crisis in 1982. Then Mexico closed its market by raising import duties to 100 percent and requiring import licenses for virtually everything. U.S. exports were consequently cut by more than 50 percent, a blow that took our exporters more than 6 years to recover from.

Based on this experience, without NAFTA, in the wake of the peso crisis, U.S. exporters could have faced a $25 billion plunge in sales to Mexico and probably not recovered until the year 2000 or later. Instead, U.S. exports to Mexico are down by less than 10 percent or by approximately $5 billion.

Indeed, NAFTA has provided a steadying hand for U.S.-Mexico bilateral trade. This year when Mexico raised duties on selected products, it exempted NAFTA goods because the agreement prohibited such actions.

Some of NAFTA's critics alleged that NAFTA itself caused the Mexican peso crisis. Such a claim is, frankly, preposterous. Mexico's financial crisis was caused by an overdependence on foreign capital and protracted, politically motivated, overvaluation of the peso.

In real terms, the peso had been depreciating since 1987 when a bungled devaluation, following a combination of political shocks, caused rapid capital flight. The peso went into a freefall.

Moreover, NAFTA did not contribute to the soaring Mexican current account deficit. Despite the fact that $20 billion of new trade took place between the United States and Mexico in 1994, the trade surplus with Mexico remained virtually unchanged—$1 billion.

Even taking the longer view during 1987 to 1994, the years of strongest trade expansion, two-way trade flows during those 7 years exceeded $500 billion, yet the United States had a cumulative trade imbalance with Mexico of less than $2 billion. That is very, very close, given such a large trade total between the two countries.

Some economists are citing the recent trade statistics and evidence of newly created trade deficits have led to the loss of thou-

sands of jobs and decline in real wages. Wrong again. While diminished short term opportunities in Mexico may have led to some dislocation of workers, since NAFTA was implemented, U.S. manufacturing employment has actually increased by 225,000 jobs, and total employment in all sectors has increased by 340,000 jobs.

Furthermore, as I previously noted, NAFTA has a safety net of over 700,000 workers whose jobs are and continue to be supported by exports to Mexico.

With respect to criticisms that NAFTA has brought about a reduction in U.S. wages, the average real U.S. manufacturing wage is half a percent higher today than it was in 1993, the year before NAFTA. American workers continue to compete successfully against less expensive Mexican or Indonesian or Chinese labor because we have higher productivity, technology and infrastructure base. That gap is widening. It is not narrowing.

Most forecasters project positive economic growth for Mexico in 1996. Frankly, I think that may not occur until 1997. Regardless of when it does, it will again realize the economic benefits that we contemplated from NAFTA.

Let me speak in my remaining time for just a moment about Latin American and Chile. Not moving with Chile's membership in NAFTA in a timely fashion would be unfortunate for a country who has long qualified for a free trade relationship with the United States.

Moreover, because of the commitments we have made to Chile, failure to move ahead would damage U.S. credibility in the hemisphere and deal a sharp setback to prospects for the hemispheric free trade contemplated by the Miami summit. This would be a major setback for hemispheric integration.

Latin America is already forming overlapping trade alliances such as MERCOSUR. Trade within and among these groups has grown rapidly. Latin American exports to other destinations within the region have increased by 100 percent in real terms since 1982.

As might be expected, the relative importance to the U.S. market to Latin America has declined slightly, given the growth rate of both global and regional trade. If we do not pursue hemispheric free trade in a timely way, by the time we do wake up to need that, Chile and other Latin American countries may have little desire or, frankly, little need to negotiate with the United States.

Chile's membership in NAFTA would be a visible acknowledgement of the dramatic way it has restructured its economy and entrenched democratic institutions. That has been a prime objective of this subcommittee and of Congress with respect to Latin America in the last decade.

Let me just say finally that while I favor a free trade relationship with Chile, I do not favor it at any political price. This Administration's demand that future trade negotiations address worker rights and environmental protection with sanctionable enforcement mechanisms is misguided and wrong.

In trying to reach agreement on the scope of future fast track authority, Republicans have tried in good faith to accommodate the Administration's concerns about these issues. We have not been able to find common ground. Nonetheless, I remain hopeful at some

point we can reach agreement on these important issues and move forward with hemispheric free trade.

Mr. Chairman, America has nothing to fear from open trade. Tariffs do not protect domestic producers. They protect ill-considered government policies, costly regulations, high taxes on labor and capital, policies that only serve to reduce the standard of living for our own citizens and stifle economic opportunities for other nations. That is what cripples American manufacturers, not foreign competition.

If you doubt this, look at Japan. There you find a powerful economic engine, but a standard of living far below that of other industrialized countries. That is why I believe we should move forward with the goal of hemispheric free trade.

It is a win/win proposition for the United States. It will advance the interest of democracy throughout the hemisphere. It will ensure long-term economic prosperity for the United States.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Kolbe appears in the appendix.]

Mr. BURTON. Thank you, Mr. Kolbe.

We have been joined by the ranking member on the Trade Subcommittee, Mr. Gejdenson of Connecticut; along with Mr. Manzullo of Illinois and Mr. Wynn of Maryland. Welcome.

We will now hear from Duncan Hunter.

STATEMENT OF THE HONORABLE DUNCAN HUNTER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Mr. HUNTER. Thank you, Mr. Chairman, and members of the committee. I want to thank you for the opportunity to talk about NAFTA with respect to Mexico and the respective free trade agreement with Chile.

As you may be aware, since the start NAFTA has failed to show even a fraction of the economic gains that were promised by many of the agreement's supporters. I can remember during the debate several years ago a number of people pointing to the relatively small surplus that we then enjoyed with Mexico and predicting that that surplus of $1 billion or so would increase dramatically under NAFTA.

Clearly, Mr. Chairman, if we are going to use the Mexican-American relationship as a laboratory in our analysis as to whether or not we extend this agreement to Central and South America, the test or the experiment has been undertaken, and the results come down definitely on the negative side.

Chile currently maintains a relatively open economy with very few protective trade barriers. The idea that somehow the U.S. economy will benefit from increased access to Chile's consumer market is very questionable.

In fact, at a briefing conducted on June 23 by the U.S. Trade Representative's office and the Commerce Department, U.S. exports related to the possible expansion of NAFTA were not even discussed.

Mr. Chairman, I believe that a much larger issue is at stake. The motivating factors behind efforts to include Chile in NAFTA is to establish a precedent for future expansion. By bringing Chile into

NAFTA, the natural next step would be to introduce various other Latin American countries into the pact. The real issue is not the opening of Chile, but the opening of NAFTA.

Now, the original purpose of NAFTA was to facilitate trade surpluses with member nations as a method of negating our trade deficits with Asia and Europe. I heard that over and over again as all the members here did in committee and on the House floor. Somehow we were going to build massive trade surpluses in our own hemisphere, and that would offset the big trade deficits with the Asian tigers.

Since the passage of NAFTA, Mexican exports to the United States are up 29 percent. During the first 6 months of this year, imports from the United States are down 12 percent. The U.S. trade surplus with Mexico has not only evaporated, but has also degenerated into what is expected to result in a $20 billion deficit by the end of the year. It is $10 billion right now.

To suggest that expanding NAFTA to the far reaches of the Western Hemisphere will result in more jobs for the United States is not supported by the facts. In 1993, NAFTA proponents promised that the presence of U.S. industry and the expected increase in trade with Mexico would provide the citizens of that country with the financial ability to purchase U.S. manufactured goods. We heard that over and over again.

Based on an artificially high peso, the Mexican economy seemed poised to expand and to explore increased trade activity. Unfortunately, in the year following the enactment of NAFTA, the actual state of Mexico's economy became painfully apparent to the world community, especially to the United States.

In 1994, the Mexican economy suffered one of its worst years in recent memory. As a result of political corruption, internal strife and investor skepticism, Mexico's international reserves plunged downward in late November from $17 billion to under $6 billion in less than 2 days.

On December 22, 1994, the Mexican government adopted a floating exchange rate for the peso without protecting its financial markets. The result was an economic collapse. Since Mexico did not have the necessary international reserves to meet payments on its Tesobonos, which are the dollar-linked government bonds, of $10 billion, the newly formed Zedillo government was forced to turn to its NAFTA partner, the United States.

On January 12, 1995, the Zedillo administration began efforts to lobby President Clinton to provide an unprecedented $53 billion in direct financial assistance. By January 31, 1995, President Clinton had agreed to funnel this assistance from primarily three sources: $20 billion from the U.S. Treasury's Economic Stabilization Fund, the ESF; $17.8 billion from the International Monetary Fund; and $10 billion from the Bank for International Settlements.

From this pool, Mexico has already borrowed over $25 billion with $12.5 billion coming directly from the U.S. Treasury's ESF. It is important to understand that these funds are not being used to rebuild Mexico's economy, as some people think, but merely to restructure the country's debt. In short, Mr. Chairman, the money is going to Mexico's past, not to its future.

In providing the recent $700 million installment payment to the U.S., Mexico attempted to show its ability to pay its debts. Unfortunately, the remaining $1.3 billion of this short-term installment will not be repaid on time.

Thus, the early payment on the eve of President Zedillo's visit to Washington was just another public relations ploy reminiscent of those which misled American opinion during the debate on NAFTA and Mexico's viability. They owed $2 billion in this installment payment. They could not make the $2 billion, so they made $700 million early and called that a real sign of strength.

With increased inflation, excessive interest rates and a shrink in economy, Mexico is clearly not becoming the economic partner NAFTA supporters originally envisioned.

The effect of these economic variables has resulted in a reduction in consumer purchasing power of close to 30 percent. Mexico's consumer cannot purchase enough American exports to strengthen the economy.

President Clinton claimed U.S. exports to Mexico are still healthy, but these are mainly components being sent to Mexican factories to be converted into goods and re-exported back to the United States.

I think that is particularly apparent in the auto area where Mexico is increasing its trade surplus in terms of completed vehicles, but still receives shipments of components to its plants located in Mexico, those being the same components that at one time were sent to American plants around the United States.

Those are now called job-creating exports because they go to a final assembly plant that is not located within the boundaries of the United States.

On the other hand, the prediction by its opponents that NAFTA would have the negative effect of industrial flight is manifesting itself right now, Mr. Chairman. So far in 1995, 47 of our nation's companies have committed nearly $500 million to do maquiladora plants in Baja alone producing goods that only can be sent into the United States.

Additionally, according to recently released Commerce Department figures, the U.S. deficit in manufacturing trade has reached $118.1 billion in the first 8 months of this year.

Although these types of figures are all too familiar, it should be noted that the small merchandise trade surplus with Mexico enjoyed by the United States in 1994 has evolved, as I said earlier, into at this point a $10 billion deficit projected to reach $15 or $20 billion by the end of this year. Mexico has now become part of the problem, not part of the solution.

Mr. Chairman, I would again like to express my gratitude for the chance to address your subcommittee on this pivotal issue. Let me just address one thing that my friend, Mr. Kolbe, brought up with respect to jobs and trade.

There is a great debate still raging as to whether our trade policies are designed to dramatically increase American jobs. I think the evidence now coming in is that they do not increase those jobs. Particularly, they do have a negative effect on real wages.

The facts are today that according to the Department of Labor statistics, in non-supervisory wages, and that is 80 percent of the

American workers, the American worker today has roughly 20 percent less the purchasing power than he did in 1973.

That means that an American worker, after the evolution of this nation's trade policies into what I think we could accurately call free trade today illustrated by the recent NAFTA deal, can walk down an aisle, push his shopping cart down the aisle in a WalMart or a K-Mart or some other merchandise store in the United States, and even though he can buy theoretically cheaper goods made in Hermacio and pull those off the shelf, he can only fill that shopping cart 80 percent as full, four-fifths as full, as he could in 1973. That is a result of the real wage deduction.

I think, Mr. Chairman, that the evidence is coming in now especially in light of an absolutely disastrous experience with NAFTA. The evidence is clearly showing that our trade policies have not accrued to the benefit of the American worker.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Hunter appears in the appendix.]

Mr. BURTON. Thank you, Representative Hunter.

We are trying to stay as close to the 5 minute rule as we can. We have allowed a little bit of latitude.

Mr. HUNTER. Take it off my score.

Mr. BURTON. Take it off your score? All right.

I will now recognize Representative Dunn.

STATEMENT OF THE HONORABLE JENNIFER DUNN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF WASHINGTON

Ms. DUNN. Thank you very much, Mr. Chairman. Thank you for this opportunity to testify.

As a member of the House Ways and Means Trade Subcommittee and as one who has traveled to Chile twice since May, I have seen with my own eyes why we should move forward as soon as possible with expanding membership in NAFTA to the nation of Chile. It is good for the United States, and it is good for Chile.

Before my first trip, I assembled a broad cross section of Washington State businesses involved in trade with Chile. Represented there was everyone from the forestry industry to trucking, from apples to computer software.

My message in a nutshell, Mr. Chairman, is that Chile is stable and economically advanced, and it is to the mutual benefit of both our countries to increase trade. I have heard Chile compared more often to Singapore and other rapidly growing countries in the Asian Pacific Rim than I have to neighboring Latin American nations.

A measure of Chile's stability is implicit in the remark of a representative from one of those Washington State-based companies who told me, with all due respect to Congressman Hunter, that "investing in Chile is less risky today than investing in California."

Mr. HUNTER. That is probably true.

Ms. DUNN. That is not saying much, is it, Duncan?

The growth of the Chilean economy over the last 20 years has been dramatic. It has been a success story by anyone's standards. Simply look at the facts. For nearly a decade, the Chilean economy has grown at a steady, average rate of 6.8 percent. We should be so fortunate.

With growth comes demand, and in Chile the demand is for U.S. products. Last year, Chilean demand for U.S. goods amounted to a contribution equivalent to $2.3 billion to our economy. Meanwhile, U.S. exports to Chile accounted for 23 percent of that country's imports.

Increased demand for U.S. products means U.S. firms will sell more goods—more Washington State apples, more Kenworth trucks, more Microsoft software and computer equipment and perhaps even more Boeing jets. That means jobs, Mr. Chairman, not only in my home state, but all over this country. More jobs result in increased economic growth for the United States and greater prosperity for all Americans.

The Chilean market is one of the most barrier free in Latin America. At this point, tariffs have dropped to an across-the-board 11 percent.

The United States is the largest investor in Chile today because Chile presents an extremely safe, low risk and profitable investment. In fact, U.S. exports to Chile have grown by well over 200 percent since 1987.

Because of widespread privatization and a dramatic savings rate, which is, by the way, around 26 percent of gross domestic product in Chile, Chile is not dependent on foreign investment or capital. This is why, as Mr. Kolbe said, unlike many countries in the region, Chile was able to insulate and protect itself from any adverse effects resulting from the devaluation of the Mexican peso. This is the mark of sound monetary policy and a healthy economic structure.

It is extremely disappointing to me personally that we have been unable to approve fast track authority. To quote the Wall Street Journal, February 3, 1995, "...there exists a very real threat that Chile's planned membership...will fall victim to the revival of NAFTA detractors..."

Who would have guessed, incidentally, that added to that threat would be the Clinton administration, the very folks who extended the invitation for Chile to join NAFTA in the first place?

Let me add that if it were not for the Administration's unwillingness to work with the Congress on fast track authority, the U.S. Congress would, in all likelihood, be poised this week to offer the positive results of its vote on fast track authority as a signal of its support of Chilean accession to NAFTA.

On the one hand, to attempt to include so many non-trade related matters such as labor and environmental regulations in a trade negotiation bill is, in my view, highly, highly inappropriate, Mr. Chairman. However, in an attempt to work with the Clinton administration in the customary bipartisan fashion accorded to trade issues, every request was accommodated, and every concern was answered.

In light of the fact that it is not the duty nor the function of the executive branch to dictate legislative policy to the Congress, there comes a point, Mr. Chairman, when the Congress must assert itself. In my view, the Administration would be well advised to put domestic policies aside and continue to promote our economy.

Mr. Chairman, in view of the successes of NAFTA, the fact that U.S. exports are up 22 percent to our NAFTA trading partners, ex-

panding the agreement to include one of the hemisphere's most competitive, most trade sophisticated, most promising countries is the next natural step.

I thank you and the committee for the opportunity to present my views.

[The prepared statement of Ms. Dunn appears in the Appendix.]

Mr. BURTON. Thank you, Representative Dunn.

Representative Kaptur.

STATEMENT OF THE HONORABLE MARCY KAPTUR, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO

Ms. KAPTUR. Thank you, Mr. Chairman and members of the committee, for the opportunity to appear this morning along with our distinguished colleagues here in the House.

I want to compliment the committee on trying to focus some attention on the impact of NAFTA, a subject that got lots of publicity prior to its passage, but since its passage very little attention by some of the very same interests that were so heavily involved in its passage.

Let me say that in my judgment, the evidence is overwhelming that NAFTA has resulted in an historic deteriorating trade balance of our country with Mexico and with Canada, significant American and Mexican job loss, declining real wages in both countries and growing instability in Mexico, which in turn has led to increased Mexican immigration to our country, illegal immigration and illegal drug flows.

Let me just say a word first about the trade balance. I remember when the debate occurred here in Hoffbauer and Choate. The Institute of International Economics went so far as to predict in the first year of NAFTA we would have a $7 billion to $9 billion trade surplus with Mexico in the merchandise area, possibly rising to $12 billion annually in the following decade.

They argued that in addition to this gigantic trade surplus with Mexico and with Canada, we would have high wage, high skill jobs in our country, that our exports would result in vastly expanded business opportunity for our companies here and that wages in all three nations would just rise beyond our wildest imaginations. Well, it sounded so good.

Mr. HUNTER. It was going to be good.

Ms. KAPTUR. It was going to be good, and we just all were to hold our chairs and hold our breath.

[Chart.]

Ms. KAPTUR. The chart that we have up there right now has two sets of arrows. The first set of arrows on the left shows in just the year prior to NAFTA's passage what the situation was in terms of trade balance or deficit with our trading partners, the red indicating about a $10 billion trade deficit with Canada at the point of passage of NAFTA and a small surplus with Mexico, which is the little blue arrow, with more of our goods going into Mexico than vice versa.

Since NAFTA's passage, what we have seen is really an implosion of over now this year close to $18 billion to $20 billion of trade deficit with Canada, which is unheard of—we have never had that

large a deficit in the last 15 years with Canada—and with Mexico a $20 billion deficit.

We have never accumulated that kind of trade deficit with either of these trading partners in the entire history of this country. In fact, our deficits now with Canada and Mexico will probably surpass our historic deficit with Japan, which is really interesting, and will inch forward in terms of our trade deficit with China.

Now, that is only in 1 year, but the magnitude of it is something. Its absence on the front pages of the newspapers of this country that were such proponents to me is a very curious development.

If we use the Administration's figures of for every $1 billion of trade you have 20,000 jobs that hang in the balance, we are talking about 750,000 jobs there on the line and at risk.

Now, let me say that in contrast to NAFTA's proponents, we have exact numbers and names of places in this country where people have already lost jobs. I submit those for the record, over 43,000 certified lost jobs in this country. There are 14,000 tomato workers and growers in the southern part of Florida. By the way, the NAFTA snapback provisions did nothing to protect them. It is a wasteland down there if you go into those tomato fields and on those docks, over 100 growers down there without any market.

There are over 2,000 workers at Briggs-Stratton in the State of Wisconsin and some of their related facilities; 240 employees at International Rectifier Corporation in Temasula, California; over 100,000 export-related jobs in Texas that did not happen as reported in the press, which we will submit for the record. The list goes on and on.

Mr. Chairman, also we will submit for the record in the State of Indiana the General Motors-Delco Electronics plant in Kokomo shifted 800 additional jobs to Delnosa, a company in Mexico; in my own state of Ohio, an additional 549 jobs from the General Motors Moraine plant; or the Emerson Electric Company in Logansport, Indiana, an additional 94 jobs and a complete shutdown there.

The lists that we have are very extensive, and I think what I find troubling is the silence and the lack of attention by those who were proponents of NAFTA to those who are being harmed by this current agreement.

If you look at the exports, our country is actually the victim since NAFTA of another overall 28 percent increase in imports from Mexico and a 17 percent increase in imports from Canada pouring over our borders just this year as compared to last year. Imports into our country have grown at a faster rate both from Canada and Mexico since the implementation of NAFTA, and our exports have not kept pace by any measure.

If you look at what we are continuing to export to Mexico, and let's just take that country, they come in three categories: electrical machinery, which has almost doubled; imported Mexican oil is coming in here; and also vehicles, almost a three-to-one ratio more vehicles.

[Chart.]

Ms. KAPTUR. I just want to show you a chart to give you a visual image of what is going on here. The first chart is prior to NAFTA's passage. It shows the numbers of cars and trucks coming from Mexico into the United States. You can see the red arrow at the

top. The little trickle at the bottom is what we were selling down there.

After NAFTA what has happened is we even got more finished goods coming in here from Mexico, truly a cheap wage export platform of goods made by multi-national companies that have been turned back into this marketplace. Why do we refuse to see what we are doing to the people of this country?

Let me just say an additional word about jobs here. We have had filed at the Department of Labor 644 petitions from firms in 48 states seeking assistance as a result of job loss due to NAFTA. In fact, some of NAFTA's biggest supporters are the very companies that have laid off workers in our country—Allied Signal, General Electric, Mattel, Scott Paper. The list is endless, and we submit it for the record.

If I might just use a little privilege here and take one additional minute, let me say that it has also been bad for wages. We were promised that wages would go up. What has happened is that productivity has gone up an additional 3 percent, but we have had an historic loss of 3 percent in terms of wages and buying power, just like Congressman Hunter said, since NAFTA's passage.

If I might submit for the record the neoclassical economic Paul Samuelson's Nobel prize winning factor price equalization theorem, he told us what would happen when two dissimilar countries like the United States and Mexico conduct trade with each other is that the wage rates for skilled labor and unskilled labor will be eventually equaled. That is exactly what is happening.

We submit the additional comments about what is happening in Mexico, which is also a serious situation which has been given short shrift in our press and shame on us as the economic leader on the continent.

Thank you, Mr. Chairman.

[The prepared statement of Ms. Kaptur appears in the appendix.]

Mr. BURTON. Thank you, Ms. Kaptur, for those remarks.

We have been joined by Mr. Bereuter of Nebraska, Mr. Chabot of Ohio, and Mr. Brownback of Kansas. It is good seeing you.

Let me start off the questioning by saying that President Clinton and the president of Mexico, Ernesto Zedillo, recently held a news conference at which they both reported that Mexico was making a pretty large repayment of the debt.

The information that has been given to us today would indicate that there is still money going south at a more rapid rate than the money that is being repaid. Can somebody explain that to me?

Ms. KAPTUR. Mr. Chairman, I would like to comment on the small down payment that was made by the Government of Mexico to our country, which was hundreds of millions of dollars, not billions of dollars. Those were then exchanged by the Government of Mexico in the Eurobond market.

I think what we are seeing here is since 1982, every time there is a Presidential election in Mexico, because of their debt and internal problems within that country, we see a fancy financing scheme invented.

Back in 1982 and back in 1987, we saw efforts by our government to influence our private banks and investors to make a difference in propping up Mexico.

What happened in 1992 was that the situation became more serious, and in the decade of the 1990's we have seen the U.S. taxpayer become the insurance company for Mexico rather than the private banks that put their money at risk during the 1980's. There has been a massive shift in responsibility here to prop up private investment that is at risk.

Mr. BURTON. So the money from the IMF, the World Bank and the Exchange Stabilization Fund is paid to Mexico in a larger amount than Mexico's repayments.

Mr. HUNTER. Mr. Chairman, $20 billion——

Mr. BURTON. The reason I am asking the question is that it appears to be a facade.

Mr. HUNTER. In my estimation, it is a facade, and here are the facts that I think support that suspicion. $20 billion in this bailout package is coming from the U.S. Treasury's ESF Fund. About $12.5 billion has already been borrowed by Mexico.

Now, Mexico, my understanding is, was due to pay back $2 billion of that loan. They paid back on the eve of President Zedillo's visit $700 million, but they are not going to be able to pay the remaining $1.3 billion that is owed.

It is like you owing $200 to Sears. You cannot make the $200, but 5 days early you walk in with $70. You say I am giving you $70, but I cannot give you the other $130 on time.

To answer your question, $12.5 billion came from ESF. They have paid back $700,000, but they owed $2 billion. My understanding is the remaining $1.3 billion will not be paid as scheduled.

Mr. KOLBE. Mr. Chairman, if I might?

Mr. BURTON. Mr. Kolbe? Maybe you can elaborate on this as well. How much money is going down to Mexico currently and in what increments? We know $700 million is coming back.

Mr. KOLBE. Mr. Chairman, I think that question is probably better directed specifically to the next panel from the State Department, who perhaps would have more specific figures as to the timing of each of the traunches, as they are called.

However, my understanding is that since the $700 million payment, there has been no further traunch, that is of a payment to Mexico, that is a cash transfer to Mexico, and, at the moment, there is no anticipation that this will take place.

The restructuring of the loans that is going on is extraordinarily important because what they are doing is restructuring very, very expensive short-term debt to long-term debt. They are able to go into the capital markets.

I would point out that in the 1982 crisis it was 6 years before they could get into the capital markets. This time they have gotten back into the capital markets in about 5 months.

They are able to get into the capital market, and they are able to refinance this short-term debt at long-term rates, which is saving them an enormous amount of money. What is going on is entirely consistent with what was planned for the use of this money.

Ms. DUNN. Mr. Chairman, let me just add that I think it is very important. The implication here is that this loan that was given by the Administration is directly related to NAFTA. It is not. It is as a result of a devaluation of the peso that comes from very bad eco-

nomic policies. I think we need to be clear to separate these two things.

Mr. HUNTER. I think you might ask, Mr. Chairman, when the next panel comes up if in fact the remaining $1.3 billion of the $2 billion loan repayment plan, if that is going to be paid on time and what that time schedule is.

Ms. KAPTUR. Mr. Chairman, might I also totally disagree with my colleague from the State of Washington? NAFTA was an investment agreement. It was there to undergird risk for private investment.

The peso crisis is directly connected to economic instability in the nation of Mexico, and the taxpayers of this country are now their insurance company. There is absolutely a direct connection.

Ms. DUNN. Mr. Chairman, I would simply like to disagree with what my colleague, Ms. Kaptur, has said. I disagree totally with what she said.

As you well know, if the issue had come to a vote on the Floor it would not have been supported by the Republic majority. What has happened is that we have made a unilateral offer to bail Mexico out of economic policies that have been very bad.

As a result, we can thank NAFTA for creating stability in that nation. NAFTA kept our trading process somewhat more stable and locked in than it would have been if we had not had Mexico as a partner in NAFTA.

Mr. HUNTER. Go ahead. Get a word in edgewise.

Mr. BURTON. This is one of the problems when you have such divergent views on the same panel.

How many jobs have been lost or gained as a result of NAFTA in the last year and a half? Make your answer short because I want to go to my colleagues.

Mr. HUNTER. I think it is very simple. They have been lost, and I'd like to take President Clinton's formula that Ms. Kaptur referred to, and that is that basically $1 billion of economic activity results in roughly 20,000 jobs or maybe 25,000 manufacturing jobs at the top end.

If you take the $10 billion trade deficit that exists as of the first 8 months of this year, and how else do you measure a trade agreement except by trade figures? If you take that figure of $10 billion and you multiply that by even 10,000 jobs per $1 billion, you have 100,000 jobs lost. If you take it by the classic figure of 25,000 jobs per $1 billion, that is 250,000 jobs lost as a result of the trade imbalance that exists today.

Mr. BURTON. Any other comments?

Mr. KOLBE. Yes, Mr. Chairman.

Mr. BURTON. Mr. Kolbe.

Mr. KOLBE. There is not a simple answer to your question. I will plead guilty, and I think both sides need to plead guilty, during the NAFTA debate to sometimes over-simplifying the arguments.

The fact is, NAFTA, like any trade agreement, is a long-term agreement. Trade is a long-term proposition. Almost one-third of our GDP now depends on trade with foreign countries. It has accounted for well over almost two-thirds of our economic growth in the last decade. Trade is extraordinarily important, and that does mean jobs.

Mr. BURTON. Before I yield to Mr. Manzullo, let me just make one real brief comment, and that is that I hope the American taxpayer can afford to wait for this long-term trade agreement to work out.

Mr. Manzullo.

Ms. DUNN. May I just make a comment on that, Mr. Chairman?

Mr. BURTON. Mr. Manzullo now has——

Ms. DUNN. I do think we need to connect, though, NAFTA with Chile. This sucking sound that we heard talked about by Presidential nominees and Members of Congress could not be made to apply to the nation of Chile. They are too far away.

Mr. BURTON. I think I agree with you on that.

Mr. Manzullo.

Mr. MANZULLO. Thank you. It is always fun when you ask questions of your colleagues.

Let me ask you some questions. What is your understanding of the average tariff rate of Chilean imports into the United States?

Ms. KAPTUR. What did he say? What was the question? We could not hear you.

Mr. KOLBE. What is the average tariff rate?

Mr. MANZULLO. What is your understanding of the average tariff rate of Chilean imports into the United States?

Mr. KOLBE. I do not have that figure on the top of my head, but I know it is relatively low now. It is quite low.

Mr. MANZULLO. It is 1 percent.

Mr. KOLBE. Yes. I was going to say two.

Mr. MANZULLO. The average tariff rate of U.S. exports entering Chile is 11 percent. With NAFTA we had the big ten-four tariff rate difference between Mexico and the United States, and now we have the big eleven-one.

Mr. HUNTER. Let me just answer my good friend, Mr. Manzullo.

Mr. MANZULLO. From Illinois.

Mr. HUNTER. That was exactly the speech or the essence of many speeches made on the House floor during the debate with Mexico to the effect that the irresistible conclusion of this disparity in tariffs would be that our slight surplus that we were experiencing at the time of the debate would grow markedly.

We would have, as Mr. Hoffbauer and Choate predicted, $9 billion/$10 billion annual trade surpluses with Mexico. Now, exactly the opposite has happened. We have $9 billion/$10 billion trade deficits with Mexico.

Mr. HUNTER. I think it is important, I would say to my friend. When you have a laboratory and you have undertaken an experiment and you have real results, I think sometimes it is important to give those results precedence over theories that in the past have not proven to be true.

Mr. MANZULLO. I understand your point, but the reason I asked the question is if what we ship to Chile is subject to an 11 percent import and what they are shipping to us is 1 percent, we stand to benefit more if tariffs are zero on both sides.

Mr. HUNTER. Yes. Let me just answer. If you listened to the first of my opening statement——

Mr. MANZULLO. But my question to you is about Chile, not Mexico.

Mr. HUNTER [continuing]. I think that Chile was taken as the nation that is perhaps most benign and has the most attractive trade situation with respect to the United States. You have listed a couple of the factors, a couple of the statistics.

I think what we are really talking about is Chile being the lead horse, if you will, for the entire region. There is more at stake here than Chile and American trade. The proponents will tell you that.

Mr. MANZULLO. And that is precisely the point because you fear that there may be a flood of Chilean imports to this country.

Mr. HUNTER. No. No. My concern is that Chile is opening the door to a much larger NAFTA and that the NAFTA in Mexico has proven to be disastrous for the United States.

Mr. MANZULLO. Duncan, I represent a city that has 980 factories. It is a city of less than 150,000 people.

Mr. HUNTER. Rockford.

Mr. MANZULLO. Rockford. That is correct. Where the deer roam, and you like to hunt them.

We are getting tremendous input from the manufacturing community. The entire 16th district of Illinois has close to 1,500 factories, making everything from food processors to fasteners to automobiles. It is across the board.

If you take isolated instances, sure you can come up with something such as what Congresswoman Kaptur said.

Ms. KAPTUR. They are not isolated, Mr. Manzullo, with all due respect.

Mr. MANZULLO. I understand your prospective, but in terms of companies that have closed and gone to Mexico, that may have happened anyway without NAFTA.

Ms. KAPTUR. Might I ask you a question, sir?

Mr. MANZULLO. We have to put all of this into perspective.

Ms. KAPTUR. May I ask you a question?

Mr. HUNTER. Don, Marcy, let me address one factor here.

Mr. MANZULLO. Sure.

Mr. HUNTER. We all know, Don, that a lot of businesses, because of what they feel to be oppressive regulations, tax structure, etc., looked at Mexico as a haven, if you will, as a soft landing place if things got tough in terms of doing business in the United States.

Nonetheless, what is really important in sales, as you know, is not gross sales. It is net sales. If you tell me that you have gone out and expanded into a new market and you have expended $2 billion, if you are talking to your CEO the CEO would say how about your home market? You say well, the other guy just penetrated my home market for $3 billion for a net loss of $1 billion.

There was a very artificial structure set in place to make NAFTA look good, and that means that if a component maker in the United States delivering to one of your prime contractors in Ohio was delivering parts and that component maker went to Hermacio, Mr. Clinton's trade advocates call that a job-producing export, even though it was basically the same, or if the prime went to Hermacio it was exactly the same production being done and undertaken in the United States.

If you acknowledge that trade deficits are bad, and I think most free trade advocates will say you do not want trade deficits, why can we not ever achieve a trade surplus?

Ms. DUNN. Mr. Manzullo, I would just like to make a comment to you, and then, Mr. Chairman, I am going to have to ask to be excused because I have another appointment in a couple of minutes.

Mr. Manzullo, my State of Washington was paired with Chile in the early 1960's under President John Kennedy in a relationship where states and nations were paired. Washington State has been doing business for a long time down there.

My folks are very, very happy with the investments made in Chile. The problem they have is that it costs 11 percent on every item that goes into Chile. I would like to see a Costco/Price Club operation set up down there. The national headquarters for Costco/Price Club is in my district. Every single product that goes into Chile now requires an 11 percent tax, if you will.

All we want to do is open up trade with Chile. They are stable. They are ready. They were invited to come in and should have probably come in before Mexico. There is a growing middle class ready for our products. That means more jobs in my state.

Mr. KOLBE. I know time has expired, but could I comment on the specific question about Chile?

Mr. MANZULLO. That is up to the Chairman.

Mr. KOLBE. Just very briefly.

Mr. BURTON. We will grant Mr. Kolbe a few minutes. Go ahead.

Mr. KOLBE. A 6.8 percent average annual growth rate Chile's economy has had. You have heard the figure used before. It is different from Mexico.

I am not saying that I do not think Mexico is good. It was, but even the opponents acknowledge Chile is more benign. It is a smaller economy. It is a very stable economy. It is one that we need to have more access to. I think it is clearly to our benefit.

Let me just say finally that nobody has said it here today, but the trade deficits are really a reflection of our national budget deficits. We have to borrow the money from overseas to pay for our budget deficits by and large because we do not have a savings rate to generate it here at home. Inevitably, that has to flow back in the form of trade deficits. It is not a very complicated economic proposition.

Mr. BURTON. Representative Bereuter.

Mr. BEREUTER. Thank you very much, Mr. Chairman. It is good to see our friends, and they are our friends. Obviously we cannot agree with our friends in every instance since they are so apart in this instance. I did hear your full statements.

I would like to take an opportunity to make my own statement, having missed the opening period of time. If our colleagues wish to respond to it, I would be happy to hear their comments.

I would commend you, Mr. Chairman, you and Chairman Roth, for holding the hearing in the first place. Today we will continue in our panels to hear a plethora of statistics and anecdotes about the benefits and costs of NAFTA, as well as the increasing information about the benefits and costs of Chile's possible accession to the agreement.

As a Member of Congress, I strongly supported NAFTA. Now I strongly support Chile's accession to NAFTA. In fact, this Member said at the time, and I will repeat it today, that in a straight-

forward fashion, it would have been more appropriate to accept Chile into a free trade agreement with the United States even before we accepted Mexico because of Chile's dramatic economic progress and liberalization.

It is very easy, I think, to get lost in all the statistics about the benefits of NAFTA or Chile's accession, but those statistics do not reveal one thing. What would have happened if we had not passed NAFTA?

There can be no doubt that many American companies have relocated to Mexico recently. Undoubtedly, many Americans have lost their jobs to cheaper Mexican labor, but that does not mean that many Americans would have kept their jobs if we had not adopted NAFTA. No, instead Americans would have lost many more low wage jobs to Southeast Asia, South Asia and other parts of Central and South America.

The situation has been greatly exacerbated, I think, as one of our colleagues said by the peso crisis in Mexico, which I would say is clearly not caused by the NAFTA agreement.

Mr. Chairman, when this body courageously adopted the Uruguay Round implementing legislation, this Member said that many opponents of that historic trade legislation were essentially saying, "Stop the world. I want to get off."

While I stand by that comment, I think it applies here today. The simple truth is that the United States and the American people have no choice but to push for expansion of NAFTA to the entire Western Hemisphere in a systematic and appropriate pace or risk being excluded from a rapidly liberalizing world economy.

Economic integration and trade liberalization is occurring in nearly every part of the world, including Europe, Asia and South America. I strongly believe Americans can compete to sell their innovative products and services everywhere in the world, provided that we are given a fair and equal opportunity without excessive Government interference.

I vigorously oppose unilaterally surrendering these future markets to our industrialized competitors in Japan and Western Europe by isolating ourselves from regional and global economic liberalization.

Accordingly, I support free trade agreements such as the enlarged NAFTA, particularly the enlargement to include Chile, which, unfortunately, is being blocked by unrealistic demands from the White House with respect to fast track legislation.

I believe that supporting these kinds of free trade agreements will ensure that American exporters are given a level playing field on which to compete.

Thank you, Mr. Chairman and my colleagues, for listening to my remarks.

Mr. HUNTER. Mr. Chairman, could I comment just briefly?

Mr. BURTON. It is his time.

Mr. BEREUTER. I yield to the gentleman from California.

Mr. HUNTER. I thank my friend, and I thank Mr. Manzullo, another great friend. I know you are going to come around to my point of view at some point, Don.

Let me just make one comment. Jim Kolbe talked about trade deficits being a function of budget deficits. Trade deficits drive budget deficits.

If you have a $60 billion trade deficit with Japan and you have 25,000 or 30,000 jobs being attached to each $1 billion of economic activity, that means that roughly 2,000,000 jobs are attendant that $60 billion trade deficit. I just used Japan as an example because it is a big number.

If you take those 2,000,000 families and you compare the time when they were paying wages or they were paying taxes through their withholding statements to the Federal Treasury and you now compare that with the fact that they are unloading the wagon and are being paid social services by the same Treasury and taking out of the Treasury, the difference for those 2,000,000 families and the impact they have on the Federal Treasury is roughly $30 billion in budget deficit.

I would offer that our experience in the last 10 to 20 years has been that trade deficits drive and create budget deficits.

Mr. BEREUTER. I thank my colleague. I do not agree that trade deficits drive budget deficits, although there is a factor in the impact upon our revenue stream.

Mr. KOLBE. Would the gentleman yield?

Mr. BEREUTER. I yield to the gentleman from Arizona.

Mr. KOLBE. What my colleague and friend from California just articulated is truly one of the most novel economic theories I have ever heard, almost as novel as NAFTA.

Frankly, I have never heard it before, and I do not think I have ever heard an economist on either side of the trade issue suggest that trade drives the domestic budget deficits. It clearly is the other way around. You have to circulate the money. You have to recirculate the money some way.

When we borrow money from overseas, you have to buy the goods in order to move that money back. That is precisely what we are doing. If we had a budget surplus, we would probably not have the problem that we have.

Nonetheless, we have been able to increase our exports very dramatically in recent years. It is very clear that it is the fastest growing part of our economy. Fifteen percent of the GDP was exports in 1970. Today it is over 30 percent. It is one-third and probably rising close to 40 percent by shortly after the turn of the century. It is an enormous part of our economy. It is the engine clearly driving the growth in this country.

Mr. HUNTER. Just one fast rebuttal. There is no economist in the world who does not contend that unemployment rates have an effect on the deficit. Unemployment rates are affected by the trade deficit. Everybody acknowledges that.

A $60 billion trade deficit with a country, presuming that your own country is capable of making some of the goods that are manifest in that deficit, definitely affects employment levels. I think Japan has been the sterling example of that illustration over the last 20 years.

Mr. BEREUTER. Reclaiming my time just for two sentences, if I could have unanimous consent, we do not agree on this one.

We are realigned on different issues in different ways, but I want to say to my three colleagues, and the fourth who was here, that I think that their energetic and articulate discussion of this multilateral trade agreement is very healthy for the House of Representatives and for the American people. I commend all of you for what you do and the energetic way that you espouse your views.

Mr. HUNTER. We are here to help.

Mr. MANZULLO. Before we go to our second panel, Congresswoman Kaptur, did you want to pose a question? I may not have the answer to it, but I wanted to give you that opportunity.

Ms. KAPTUR. I thank you very much, Mr. Chairman.

The only point I wanted to make and then pose the question to the panelists is if you look at your own districts and you look at what has happened to people's buying power in this country since the late 1970's, we have not had an expansion in purchasing power for the vast majority of families.

If you look at the point at which that decline began, it started with the Uruguay Round back in the late 1970's. Every succeeding so-called liberalization round of trade, whether it was the Tokyo Round, whether it was the new GATT or whatever, we have fallen deeper and deeper in the hole in terms of trade deficit, but also sluggish and declining wages.

I wanted to just ask our colleagues in the generic here to check on what has happened to the buying power of families who work in your district because if you look at wages going from $15 an hour in many cases to $5 an hour, Medicare's problem is a problem relating to the payment in from payroll taxes under FICA. When you are not earning as much per hour, you are not paying as much in. A $15-an-hour job you pay $1.50 an hour in to FICA. If you earn $5 an hour, you pay about 50 cents.

A lot of what is happening in this country is related to the declining wage issue that Congressman Hunter referenced, and I would just encourage the panel to take a look at what is happening to wages in your area.

Mr. MANZULLO. Let me take a stab at that, and then we can go on to the second panel.

In 1950, a family of four had an average Federal tax burden of 5 percent. In 1993, that grew to 24.5 percent. If a husband and wife are working today, one of those partners is working solely to pay taxes.

According to a chapter called Generational Forecasts that appears in the U.S. budget, by the time children born in 1992 enter the work force, unless something is done to bring this budget deficit under control, those children will be paying in combined state, local and Federal taxes between 84 and 94 percent of their salary.

Exports, as far as I am concerned, and imports are totally irrelevant to taking home money. The problem is that the American people are paying too much in taxes. That is the problem. I guess you asked a question, and that is my answer to it.

I would like to move on to the second panel, if that is OK.

Ms. KAPTUR. I thank the gentleman. I was not going back to 1950. I was in the 1970's, but I will certainly look at your numbers for the 1950's.

Mr. MANZULLO. I appreciate it. Thank you.

Mr. Bereuter.

Mr. BEREUTER. I thank the Chairman for yielding.

I would say to the gentlelady that you shouldn't link, as you did, this difficulty which you say began in the late 1970's to the Uruguay Round. The Uruguay Round was a 7-year process, and did not start until the 1980's during the Reagan administration. It did not start in the late 1970's during the Carter administration.

Mr. KOLBE. It did not go into effect until this year.

Ms. KAPTUR. No, no. The original one way back——

Mr. BEREUTER. That was not the Uruguay Round. That was the Tokyo Round.

Ms. KAPTUR. I have to go back to my chart and look. I think it was like 1974 or something or 1978.

If you look at the different trade treaties that were put in place and then you look at what has happened to wages in those intervening years and to the trade deficit, it is very clear what is happening with the downward pull on wages, which is irrespective of taxes, by the way.

Mr. MANZULLO. We appreciate that. Thank you very much.

It is always very interesting to see how trade issues fall among Members of Congress. It has absolutely nothing to do with political parties. This is a good policy discussion, and I really appreciate it.

Mr. HUNTER. Just common sense.

Mr. MANZULLO. Just common sense. Thank you.

If the second panel could come up now, we would appreciate it. The second panel consists of three witnesses from the Administration. They are The Honorable Ira Shapiro, Special Negotiator for Japan and Canada in the Office of the U.S. Trade Representative; The Honorable Alexander Watson, Assistant Secretary for Inter-American Affairs with the Department of State; and William Barreda, Deputy Assistant Secretary for Trade and Investment Policy at the Department of Treasury.

We will start off with Mr. Watson. I believe you have a previous engagement. Is that true? Who wanted to go first?

Ambassador SHAPIRO. Actually, Mr. Chairman, if I could go first?

Mr. MANZULLO. Ambassador, please go ahead.

STATEMENT OF THE HONORABLE IRA SHAPIRO, SPECIAL NEGOTIATOR FOR JAPAN AND CANADA, OFFICE OF THE U.S. TRADE REPRESENTATIVE

Mr. SHAPIRO. Thank you, Mr. Chairman. I shared your sentiment about the vigorous debate that went on. It is one of those subjects when not only do the Members of Congress do justice to the vigorous debate, but we sit in the front row and want to jump in at all moments.

I am not sure that in my few minutes I can summarize my testimony and also respond to some of these points, but I am going to try anyway because there were some important points made.

I would like to put my full statement in the record and just make a few key points.

Mr. MANZULLO. Without objection.

Mr. SHAPIRO. First, Mr. Chairman, while my responsibilities now are primarily Japan and Canada, I was General Counsel for 2

years when Ambassador Kantor took over in 1993 and 1994, so I was intimately involved in the NAFTA at that time.

My first point would be that trade expansion and agreements to expand trade are, in our view, essential for the United States to build the kind of economy that we want for our workers and for the children that come into the work force in the coming years.

If there is one thing we can be sure of, it is that the good old days when we could confine our interest to our domestic market and prosper are long gone. We are a mature economy with only 4 percent of the world's population. Our ability to prosper in this world depends on our ability to sell our products and services throughout the world to the other 96 percent of the population.

Fortunately, I believe that we are well situated to prosper in that kind of world. We lead the world right now in everything from aircraft to agriculture. Our movies and our sound recordings are sought all over the world. We are at the cutting edge of computers and software, and some of the industries that were regarded as in danger in the 1980's, industries like semiconductors, steel and autos, have surged back as world class competitors.

Congressman Hunter and Congresswoman Kaptur pointed to 1973 as an important time in which U.S. prosperity started moving in the wrong direction. I think they are correct about that. There was a long period of time in which the United States did not adjust to the need to compete in the world. We stayed with the policies of the 1950's and the 1960's far too long. You can see a decline in wages and living standards.

In addition, our view of trade showed a willingness to be an open market on our own, but not worry about opening foreign markets. That combination of policies and a failure to adjust to a changing world cost us for a long period of time.

Mr. Chairman, I learned my trade policy working for Senators from Wisconsin, Missouri and West Virginia in the 1970's and 1980's, so I know something about the kind of job losses that companies and our workers went through during that period of time.

What we have tried to do in this Administration, and what our companies and our workers started doing some years ago, is adjust to that competition. What we need, in addition to the talent of those companies and workers, is open markets in which to sell.

Since this President's election, the cornerstone of our trade policy has been a commitment to open trade, but with reciprocity. We welcome the products and services and investments from other countries, but we insist that we are going to get our products, services and investments into those other countries.

We have sought to do that through the vigorous use of our trade laws, but we have also done it by negotiating trade agreements. That is what our efforts have been about. That is really the essence of what NAFTA and the Uruguay Round were about.

We start out as a more open market. Therefore, if we can negotiate trade agreements with others, we are bringing down their barriers and opening their markets to us. That was the core justification of NAFTA, and it remains the core justification of what we are advocating for Chile and Latin America.

Let me say, Mr. Chairman, that our trade policy has been bipartisan to the core. We could not have done it without Republican support, as you well know.

No. 2, we see evidence that our strategy is working. During the past 30 months, we have negotiated about 170 trade agreements, including NAFTA and the Uruguay Round. At the same time, our exports have expanded almost 30 percent, 16 percent in the last year since the Uruguay Round took effect.

An increasingly competitive economy has generated 7,000,000 new jobs since December, 1992, more than 90 percent of those in the private sector. Mr. Hunter commented on unemployment. It has gone down from 7 percent to 5.6 percent. In Ms. Kaptur's State of Ohio, unemployment is now 5.2 percent, and Ohio is living through an export led boom across the board.

Mr. Chairman, I would like to introduce in the record, and you may be familiar with it and Mr. Bereuter may be familiar with it, a Business Week story last year on how the midwest was playing a critical role in the global economy. The article shows that the midwest is really leading our resurgence in manufacturing and that resurgence was led by our ability to export.

Consequently, while I agree with some of their concerns about where we have been the last 20 years, I believe the policies the President and this Congress have put in place on trade are the solution to this problem, and it is already working.

Let me add one other thing because I have worked with Ms. Kaptur on auto parts when I negotiated with Japan, and I think opening those markets is critically important to us. When she looks at the trade with Mexico and draws this bleak picture, what she is ignoring is that from 1990 to 1994, we had an incredible resurgence of our auto industry and our auto parts industry.

One reason we imported parts from Mexico was because we had such a demand for parts. The U.S. parts industry was operating full out, and the Mexican imports supplemented that production. In a 4-year period, our auto parts production in the United States went from $157 billion to $229 billion, up $70 billion. We started out that 4 years making 2.7 million cars less than Japan. Four years later, we were manufacturing 1.7 million cars more than Japan. That is why there has been a demand for auto parts.

It is hard for me to add much to what Congressman Kolbe said with respect to NAFTA. We believe that NAFTA was the right thing to do, and we believe that it has been successful despite the most difficult circumstances that have confronted Mexico.

NAFTA trade went up 17 percent the first year, and in the second year when Mexico went into a very deep recession our exports fell much less than one would have expected. Our exports fell less than Japan's and the European Union's.

NAFTA locked in the reforms in Mexico. Mexico continued to reduce their tariffs on our trade while raising import barriers on other countries. As a consequence, we went from 70 percent of Mexico's imports to 73 percent. I believe that the test of a trade agreement are the worst times you can put it through. I think NAFTA has come through under those adverse circumstances.

The third point I simply want to make is the case for moving ahead with trade expansion into Latin America is very strong. This

is the second fastest growing region in the world. It has witnessed an incredible transformation to a market economy and to increasing democracy throughout the continent. We have increased our exports rapidly there, but there are great opportunities ahead for us. We need to move ahead to lock in those reforms.

Moreover, I think that what was said by one of the witnesses, or perhaps it was one of the members up there, is entirely correct. If we do not move ahead, others will. The subregional trading arrangements are beginning to proliferate, and they are not going to proliferate to our advantage.

The Europeans and the Japanese are very anxious to be a part of the second fastest growing market in the world, and we run the risk of forfeiting the opportunity to take the lead and to continue opening markets for our companies and our workers.

The last thing I would say on this, Mr. Chairman, is we have been working with all the countries of the hemisphere in the aftermath of the Summit of the Americas. Most of them will not be ready for full-fledged free trade agreements for some years, but we have been working with all of them to try to upgrade their disciplines and to open their markets.

To make this process real and to get the maximum benefits for the United States, I believe we have to move ahead with NAFTA accession, and we have to start with Chile, which has been promised a trade agreement with the United States by two presidents, one of each party. Chile's accomplishments economically have been referred to by others, and I am not going to review them again except to say that they have been extraordinary.

We need to move ahead both because Chile deserves the opportunity to negotiate an agreement with us, because it is the stepping stone to the rest of Latin America and our credibility in carrying forward that agenda is very significant.

My last point is that we have valued the bipartisan trade policy that we have had. In your absence, Mr. Chairman, I referred to the fact that we could not have done anything that we have accomplished without bipartisan support.

We are asking the Congress to grant the President the fast track authority to continue moving ahead. I know it is a controversial subject. Ambassadors Kantor and Barshefsky are working closely with the Congress to try to fashion a fast track proposal that can be supported on a bipartisan basis. As you know, we have an interest in continuing our work in environment and the labor areas. Thirty-four nations in Latin America at the Summit committed that that should be part of trade expansion in this hemisphere, but we are asking for it in the sense that it is trade-related items of environment and labor.

I think that it is a challenge for us, but it is a real opportunity for Congress and the President to work together to formulate a fast track proposal that will allow us to keep going forward.

We are going to have enough differences on a partisan basis without question in the next year, but on trade our progress has been bipartisan, and we hope to keep it that way. We ask for your continued support for our moving ahead.

[The prepared statement of Ambassador Shapiro appears in the appendix.]

Mr. BURTON. I know you have time constraints. Mr. Manzullo and I have a couple of questions.

Mr. SHAPIRO. I am here as long as you want.

Mr. BURTON. I thought Mr. Manzullo indicated that you and some of the other panelists have to leave.

Mr. SHAPIRO. They may have to, but I am staying.

Mr. BURTON. Mr. Watson, you have to leave? Is that correct?

Mr. WATSON. Thank you, sir. We do have the swearing in of one of your former colleagues, Bill Hughes, as our new Ambassador to Panama. I wanted to attend that ceremony.

More important even than that is that I want to be responsive to the committee. We thought that the best thing to do would be, since this is basically a trade-focussed hearing, was to have Ira open up, and then I would go second. I can stay here as long as is necessary. Bill will excuse me.

Mr. BURTON. Then we will proceed.

Ambassador Watson, do you want to go next?

STATEMENT OF THE HONORABLE ALEXANDER F. WATSON, ASSISTANT SECRETARY FOR INTER-AMERICAN AFFAIRS, DEPARTMENT OF STATE

Mr. WATSON. Thank you very much. Thank you, Mr. Chairman.

I would request, sir, that you include in the record my longer statement.

Mr. BURTON. Without objection.

Mr. WATSON. I would like to make just a few remarks that pick up on some of the things that other witnesses have said.

I want to put the trade issue in a little bit broader foreign policy context for the committees, if I may. Clearly, this is a time of unparalleled progress and hope in our hemisphere. I think you have heard that from some of the other witnesses. It offers unprecedented opportunities for strengthened cooperation on a wide range of issues vital to the United States.

Last December's Summit of the Americas consolidated the convergence of goals that have been developing over the last few years between the United States and Latin America, and the commitment to negotiate a Free Trade Area of the Americas, FTAA, by the year 2005 caught the imagination of the hemisphere not only because it will increase growth, but also because it symbolizes the new common philosophy of the hemisphere of free enterprise, decisionmaking by markets, not governments, growth and opportunity. It also powerfully supports the profound democratic and social transformations now underway in Latin America.

As President Clinton said when he hosted President Zedillo here in Washington a couple of weeks ago, "The stronger our trade, the greater the well being of all our people, the deeper our cooperation and the better we will be able to fight together our common problems."

The United States has much to gain from a mutual opening of markets in the hemisphere, as others have pointed out. Already we export almost as much to Latin American and the Caribbean as we do to the European Union. It is a fast growing market. From 1990 to 1994, U.S. exports to the region increased by $36 billion com-

pared to an increase of only $3 billion to the countries of the European Union.

Latin America and the Caribbean is a good partner with a strong commitment to market economics, a solid growth outlook and a strong orientation toward the United States. It has moved far toward opening its markets, but Latin American tariffs are still about four times higher than our own.

Further growth and liberalization would clearly benefit the United States. The movement to freer trade is now at a point which requires our active engagement. Further liberalization in Latin America almost certainly will take place primarily through international negotiation rather than by unilateral government decisions as has been the trend until now.

Subregional integration arrangements now cover virtually every country in the hemisphere. In addition, Latin America is forming links outside the hemisphere with APEC and with the European Union. As I think Mr. Bereuter pointed out, absent U.S. leadership in structuring a liberalization process, the balance of interest and commitment in Latin America could well start to shift away from us.

Turning to our experience with NAFTA, I believe the record shows that it is working both for Mexico and the United States. Despite Mexico's current economic difficulties, our exports are still above pre-NAFTA levels with every expectation of renewed growth as the Mexican economy rebounds.

U.S. exporters have actually increased their share of the Mexican import market this year, as Ira pointed out a few minutes ago, and NAFTA gave U.S. exporters a privileged position in the Mexican market, which strengthened when Mexico raised tariffs on some imports from third countries and continued to strengthen as Mexico's barriers to its NAFTA partners are phased out in accordance with NAFTA's schedule.

Some have argued that Mexico's current economic problems are the result of NAFTA. This is patently untrue. Mexico's problems resulted from its government's macroeconomic policy decisions last year, not from NAFTA. The market-based reforms locked in by NAFTA are restoring investor confidence in Mexico and have already allowed Mexico to return to the financial markets in 7 months rather than the 7 years it took to recover from the 1992 crisis.

NAFTA is helping to rebuild the condition for Mexico's growth, which is strongly in the interest of both Mexico and the United States. It clearly benefits us when Mexico, our neighbor, major trading partner and close friend, has a healthy and dynamic economy.

Let me touch for just a minute on Chile. Chile's accession to NAFTA will benefit both the United States and the hemisphere. Chile is an example of the rewards of democratic and market oriented policies. Both Presidents Bush and Clinton committed the United States to negotiate free trade with Chile, and the discussions initiated earlier this year have been promising.

While Chile is certainly not a huge market for the United States, neither is it insignificant. Last year, for instance, we sold more to Chile's 14,000,000 people than we did to India's 920,000,000 people.

Chile is well prepared to fulfill the commitments of the NAFTA. It is one of the most open investment and trade regimes in the world. Its 12-year record of economic stability and unbroken high growth with low unemployment, low inflation and decreasing poverty give us confidence in its economic policy leadership.

In light of Chile's remarkable achievements, Chile's entry into NAFTA would not only demonstrate U.S. support of political and economical reform, but would also encourage a higher level of trade discipline throughout the hemisphere. This is very important. Chile is the logical next step as we pursue the Free Trade Area of the Americas.

To conclude, Mr. Chairman, Latin America and the Caribbean are of major importance to the United States. Almost every problem which confronts U.S. communities today—crime, drugs, jobs, the environment, just to name a few—has some transnational aspect that is reflected in our hemisphere.

The question before us is not whether to cooperate with our neighbors, but how to structure that cooperation most effectively. Trade is a crucial part of our relationship with Latin America and the Caribbean, and the FTAA will clearly benefit U.S. commercial interests.

It is far more than just a trade arrangement. It symbolizes the new relationship between the United States and Latin America as equal partners with common values and practical means of cooperation to achieve common goals.

Thank you very much, Mr. Chairman.

[The prepared statement of Ambassador Watson appears in the appendix.]

Mr. BURTON. Thank you, Ambassador Watson.

Secretary Barreda.

STATEMENT OF WILLIAM E. BARREDA, DEPUTY ASSISTANT SECRETARY FOR TRADE AND INVESTMENT POLICY, DEPARTMENT OF TREASURY

Mr. BARREDA. Thank you very much, Mr. Chairman.

After the first panel and the statements of my two colleagues, there really is very little left for me to say, so I will summarize my statement.

In my statement I mention again why it is in the U.S.' interest to negotiate a free trade area with Chile and also that NAFTA has very definitely been in our interest. I mention Chile's strong economic performance, which has been touched on by many of the members here.

I would underline, though, that some of the noteworthy aspects of Chile's performance have been its dependence on and its increasing use of, the private markets. By privatizing their social security system, they have created huge savings and financial markets. They are continuing to look at privatization of such areas as roads and tunnels. The imagination and the excitement and the use of the market, I think, make them an exciting prospect for a partner.

Also, having a negotiation with Chile and having Chile in NAFTA will encourage these types of policies in the rest of Latin America. These are the types of policies, Mr. Chairman, which will generate U.S. exports and jobs.

I mention, because it is such a Treasury interest, Mr. Chairman, our experience in financial service negotiations in the NAFTA. Mexico was a closed market in financial services when we started negotiating the NAFTA. We were able to negotiate an opening with some transitory safeguards.

I am also pleased to report that Mexico is living up to those obligations, despite the hard times. Some 107 foreign financial institutions have applied for entry into the market because of NAFTA liberalization, and some 97 of those applications have been approved, Mr. Chairman.

Chile's financial markets are generally open, so we think it would be reasonably simple to negotiate financial service liberalization as part of NAFTA.

Another area of Treasury interest is a tax treaty. We think we would need a tax treaty to compliment the NAFTA negotiation to ensure there was not discrimination in the tax area.

Mr. Chairman, there has been some mention of the support package put together, and I would like to make a few comments on that.

First, as has been said, the balance of payment difficulties of Mexico were not caused by NAFTA. They were caused by macroeconomic policies, as Ambassador Watson has said. They did pose serious threats to vital American interest, and that is why we acted. We acted to ensure protection for U.S. exports, for U.S. jobs and for the security of our border.

There was also another aspect of the Mexican crisis, the chance of a spillover. In the 1980's, we saw the beginning of the debt problem in Mexico spread to the rest of Latin America, and we really lost 10 years of U.S. export growth.

I think the most important thing is to say that this package and Mexican policy measures are working. Mexico is doing its part. It has run a tight macroeconomic policy and a tight monetary policy and is continuing its liberalization and privatization programs.

These two programs working together are working. The financial situation improved dramatically. The Tescbonos have been virtually paid off. Less than 10 percent are left. International reserves have risen. As I mentioned, macro policy is tight, with a budgetary surplus of some 2.1 percent of GDP in the first half of 1995.

Inflation has fallen fast. The Mexican stock market is bouncing back. The peso has traded relatively steadily in the last few months. Again as was mentioned, Mexico was able to return to the international capital markets after 7 months, not 7 years this time.

The contagion of the Mexican crisis to other Latin American countries has not taken place. There was a worry at the beginning, but I think the record shows that these countries too have stabilized, and our assistance to Mexico has helped make that happen.

Another important point, though, Mr. Chairman, is that NAFTA has also helped us in this process. The principles and the concepts of NAFTA have guided Mexico in their policy responses. They have not fallen back into statism, closing markets and stopping flows across borders. They have continued with their market opening, and NAFTA, of course, has protected our own interests, as we mentioned, as tariffs kept being cut on our exports while they were raised on those of other countries.

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In short, Mr. Chairman, I know it is a controversial program, but I think the record is showing it was the right decision, and it is working.

Thank you very much, Mr. Chairman.

[The prepared statement of Mr. Barreda appears in the Appendix.]

Mr. BURTON. Thank you, Mr. Secretary.

We have been joined by Dana Rohrabacher of California, a member of the committee as well.

Chile is a good, stable economy and would be a valued trading partner. I believe in free trade and fair trade, and therein, as Shakespeare said, lies the rub.

There is no question about Chile being a better trading partner than Mexico and probably should have been the first nation that we negotiated with for a free trade agreement, but hindsight is always 20/20.

The NAFTA agreement, from my perspective, was flawed. First of all, the trade barriers or the tariffs do not come down consistently on both sides. In many cases, the import tariffs on the Mexican side stay high over a 15-year period, while on the U.S. side, they come down over a period of about 5 years.

Another area of concern was acceding to an international tribunal (a Mexican, an American and a Canadian), the ability to impose penalties and to resolve trade disputes without any recourse by an American businessperson in our U.S. Courts. I thought there was a question of constitutionality there.

You can respond to that if you like, but those were a couple of my concerns.

If we are going to be negotiating a trade agreement with Chile, it seems to me that it might be advantageous to look at it from a bilateral position rather than including it into the NAFTA quagmire. I use that term. I know others would not.

We do have a huge trade deficit with Mexico and Canada over the past year or year and a half, and it seems to me that Chile would be a valued trading partner. If we could work out a bilateral agreement that would solve our problems and have the two countries resolve trade disputes and penalties and everything else, I think that would work.

I believe there are going to be some real problems putting Chile into the Mexican/Canadian/American equation that we have with NAFTA. You can comment on that if you like.

The other issue is the Exchange Stabilization Fund. You spoke about that and the total of $53 billion in American and international assistance to the IMF and other financial institutions that Mexico has received.

There is no doubt in my mind that a floundering economy, an economy that has devalued its peso like Mexico has and is having severe economic problems, would start looking a heck of a lot better with an infusion of $53 billion in capital. It is no wonder to me that the economic situation has stabilized in Mexico with that huge infusion of capital.

I was one of the five people that the Speaker of the House asked to develop an agreement that could be worked out with Mexico in

order to use part of the Exchange Stabilization Fund and other financial markets or investments to help stabilize that economy.

We had some criteria that we wanted to be put into an agreement. Number 1: that Mexico would invest or put in American financial institutions 10 percent of the loan coming from the Exchange Stabilization Fund or whatever fund we decided to use, so that the American taxpayer would be protected. Mexico objected to that.

We did not want them to give any of our assets or our financial loan to Cuba because of the U.S. embargo. They did not want to agree to that.

What happened was the Clinton administration unilaterally took action using the Exchange Stabilization Fund, which many of us thought and still think was illegal because it is supposed to be used to support the dollar rather than to support foreign currencies. I am going kind of all around the barn here just showing you some of my concerns.

I guess the comments I would like to make, No. 1, is it is no wonder that the Mexican peso is bouncing back and their stock market is stabilizing with this large infusion of American capital, but we still have a $20 billion trade deficit staring us in the face from Mexico and an $18 billion deficit from Canada. We still have problems with trade barriers coming down disproportionately on one side or the other.

I would like for you to comment on why do we not look at a bilateral agreement with Chile, who would be a valued trading partner? We could work that kind of agreement out. I think we could get it through Congress in a relatively short period of time.

Then, if we work out our problems with NAFTA, we could throw all our trade agreements into a multi-national trade agreement that would be more equitable. Right now with the problems we are having with NAFTA, I think you are going to have a tough fight on the floor of the House. You may get it passed, but it will be a very difficult fight.

I will let any of you gentlemen comment that would like to on that.

Mr. SHAPIRO. Mr. Chairman, let me start, and the others can chime in. I will try to address some of those concerns.

Respectfully, in some of the areas we may just disagree, but I will try to supplement the record in those areas to try to make the case more strongly.

With respect to the balance of concessions and the phaseouts that you have referred to, when we came up to the Hill during the NAFTA implementing process, I remember the Ways and Means Committee was quite surprised that very few changes in U.S. law were required, and virtually all the changes of law that were required were on the Mexican side.

Mexico had to make significant changes in their trading system because they were not as open as we were. That goes for everything from intellectual property to standards.

With respect to tariff cuts, those were vigorously argued and negotiated. We did not get all we wanted, and I can point to a couple of areas that I wish the tariffs would phase out faster, but I think

there was more than a fair balance in terms of which tariffs were reduced immediately, 5 years and then up to 15.

We kept long tariffs on a number of our sensitive items. They had to make immediate changes in a number of their sensitive items ranging from autos to agriculture. I would be happy to document that, but I do not think that it is accurate to say that the concessions were unbalanced.

With respect to what you have referred to as the NAFTA quagmire, I need to say a word about trade deficits here. Obviously we all look at them, but the overall trade with Canada, for instance, is way up in the last few years, imports and exports.

The integration of the Canadian market between the United States and Canada is one of the reasons that we have been doing so strongly in manufacturing and exporting products like automobiles and are so strong in our market because of this increasing integration.

The trade deficit number is something we are all going to look at. When I listened to Mr. Hunter, I was reminded that we had a $28 billion trade deficit, which was a quite low trade deficit, in 1982. We also had almost 11 percent unemployment. We were in the depths of the 1982 recession.

To some extent, when our economy is growing, whether it was during the Reagan terms or whether it has been the last couple of years, trade deficits have been a part of it because we consume domestically, and we draw in products from abroad.

At the same time, our exports have been expanding, as I said, 16 percent in 1 year, almost 30 percent the last 3 years. I think one has to look at the overall economic activity.

With respect to a separate agreement——

Mr. BURTON. But we still have a $100 billion trade deficit with the rest of the world, which is very bad for the U.S. economy over the long term.

Mr. SHAPIRO. Believe me, I am not a defender of the trade deficit. I have been working hard on the Japan question, but I was trying to indicate a certain correlation there. It has to be looked at in terms of the overall economic picture.

With respect to a separate agreement with Chile, obviously this comes back to a different view that we have on NAFTA, but we think there would be a real significant problem with negotiating separate arrangements with other countries, first of all because the NAFTA standards are quite high in many areas, and we would like to bring Chile up to that with respect to intellectual property, for instance.

The difficulty of having different standards and proliferating standards with differing trading partners I think is a significant one. We have looked at it, and we did look at that question and have come down in favor of the question of trying to negotiate NAFTA accession. We also have the support of Canada and Mexico for going on that route.

The last question that I will respond to, and then I will turn it to Mr. Barreda to discuss the financial package, is with respect to these international tribunals. I know that there is skepticism up here about them in certain areas. I would only say that we see some benefits in international tribunals in resolving disputes be-

cause often times our trading partners are not living up to their obligations.

To give you an example, in the first Chapter 19 case which has to do with Mexico's anti-dumping and countervailing duty laws, a panel ruled that Mexico had not complied with its obligations and had improperly collected duties from Bethlehem Steel and from USX, and emphatically decided that those duties had to be refunded. The U.S. steel manufacturers won the case. We win a good many of these cases, and we are going to continue trying to win them.

Mr. BURTON. I do not want to monopolize this, but the appeal——

Mr. SHAPIRO. No. I was monopolizing.

Mr. BURTON. The appeal process is what concerns me. I have no problem with a three member panel coming up with a conclusion, but for an American businessman who may be fined a great deal of money to not have an appeal process through American courts really steps on their constitutional right.

Mr. Barreda.

Mr. BARREDA. Just a very minor comment, Mr. Chairman. We understand your views. As you know, the Administration's first approach was to come through the Congress. It was not possible to bring that to fruition, and the President had to act. We acted on that. We certainly respect your views and understand them.

Mr. BURTON. Mr. Bereuter.

Mr. BEREUTER. Thank you, Mr. Chairman. Gentlemen, thank you very much for your testimony.

Mr. Barreda, I would like to ask your opinion as to whether or not the United States or Mexico would have reacted any differently to what I will call the peso crisis if there had been no NAFTA agreement?

Mr. BARREDA. Mr. Congressman, the reason we acted was not because of NAFTA. It was, as I said, because it was a very large country and very important to us, very important to our trade, important for many of our other relationships, and because of the worry of contagion.

Mr. BEREUTER. That is helpful, but my question was would we have reacted any differently if there had been no NAFTA agreement?

Mr. BARREDA. Since the NAFTA was not really the reason we were acting, I think we would have reacted very similarly, yes. That is speculation on my part, however.

Mr. BEREUTER. This is, I think, primarily in your subject area, but if the other two gentlemen have something to say on that subject you are welcome to express your views.

Mr. Watson.

Mr. WATSON. Thank you, sir. I think you asked when you asked your question would the United States or Mexico react any differently.

Mr. BEREUTER. Any differently if there was no NAFTA agreement.

Mr. WATSON. Of course this is hypothetical and speculative, but I think that Bill is right. The national interest of the United States was such that we would have had to have acted in some way to

prevent the damage that could occur to our economy and to others around the world.

I think that history shows that Mexico reacted very, very differently in this case than they did in 1982, as I think Jim Kolbe pointed out most articulately this morning.

Therefore, I think NAFTA really did make a difference in terms of locking in and limiting, in a way, Mexican options and keeping them in the open market framework as they sought a solution to their problem. That allowed them to go back in the market quickly, and it certainly had an impact on our exports to Mexico which, if history is any indicator, would have dropped considerably more had we not had NAFTA.

Mr. BEREUTER. You heard the comments from the first panel, of course. A couple of my colleagues on that panel, only two, have very strong views that NAFTA had something to do with the precipitation of the peso crisis. I do not believe that is the case, and I wanted to have your views on that.

I would like to move to trade now and focus perhaps on Ambassador Shapiro first. I believe it is true that Chile is a relatively new member of APEC, the Asia-Pacific Economic Council, which I think is an interesting step on their part and should give us an indication that there are other trade blocks being created, and we need to be cognizant of that fact in preserving our own best interest and our own national interest.

What is the status now of Chile's discussion to join the Southern Cone common market, the MERCOSUR, and what should we think about that?

Mr. SHAPIRO. Mr. Bereuter, Chile has been pushing ahead on a variety of fronts. They have been very active with respect to MERCOSUR, as well as looking at issues with respect to the European Union.

My general view is, as I indicated in my testimony, we have an opportunity and we are the natural party to take the lead in trade expansion in Latin America, but there is absolutely no doubt that nobody is waiting around.

They are generating a great deal of energy internally through MERCOSUR. Chile is interested in that. They are considering a trade agreement with the European Union. Chile, in fact, as you know, has a rough balance, though not an exact balance, of trade with respect to the United States, the European Union and Japan.

I think it underscores for us all that Chile is a valuable trade partner that a lot of countries are interested in and the need to move ahead.

Mr. BEREUTER. Are there conditions or requirements for membership in MERCOSUR that would cause Argentina and Brazil and Uruguay, for example, to be easier to integrate into NAFTA or into some kind of multi-lateral trade arrangement with the United States, or is it mainly an unconditioned kind of agglomeration of interested countries?

I guess in short, does MERCOSUR work in our interest as long as eventually we take these people into liberalizing trade pacts with the United States. Or, does it have no impact upon their eligibility for our consideration to bring into a liberalized trade pact?

Mr. WATSON. Mr. Bereuter, maybe I could begin, and Ira could follow.

Our view so far first in terms of Chile's and working out an arrangement with the MERCOSUR countries is that they have been talking a lot. It looks like Chile will not actually enter MERCOSUR. Its tariffs on many items are already lower than the MERCOSUR countries, so they have to work out some sort of reciprocal arrangement there.

To the extent that an arrangement like that is not trade restricting and in fact is trade enhancing and in fact brings tariffs down in all of the countries, I think it is in our interest and certainly we would not be opposed to that.

Also as we look at the MERCOSUR, the same conditions and criteria apply. They are moving forward very carefully in a different kind of arrangement. It is a much more complex arrangement than the NAFTA is because they have a common external tariff. They have a customs union at the end of the road, and they are not there yet.

Once again, we are not fearful of that as long as it is trade enhancing, and tariff barriers are brought down across the board and we are not discriminated against because anything that moves, as I was trying to say in my opening remarks, in favor of trade liberalization in a part of the world where 40 percent of their imports come from the United States really has to be of benefit to us.

We just have to watch and make sure that we are not discriminated against in these processes.

Mr. BEREUTER. Thank you.

Ambassador Shapiro, did you want to comment as well?

Mr. SHAPIRO. No.

Mr. BEREUTER. All right. Thank you, Mr. Chairman.

Mr. BURTON. Thank you, Mr. Bereuter.

Mr. Engel.

Mr. ENGEL. Excuse me. Would you mind if I yield to my colleague?

Mr. BURTON. Mr. Rohrabacher.

Mr. ROHRABACHER. Thank you. The only reason why I said that is I do have to go. I appreciate Mr. Engel——

Mr. BURTON. We always honor those with nice beards first.

Mr. BEREUTER. I would like to just ask, No. 1, about the Mexican bailout. How much money eventually came from U.S. sources, whether directly or indirectly, to help Mexico out of that crisis?

Mr. BARREDA. The U.S. Treasury out of the Exchange Stabilization Fund made available $20 billion. Mexico has drawn from the ESF and the Federal Reserve $13.5 billion and has paid back $1.7 billion.

Mr. ROHRABACHER. Not to mention other international organizations for which we guarantee their involvement.

Let me just say that I understand why some people might put the NAFTA and the bailout together. I do not. I do not think that they are synonymous. I think the bailout was a whirlwind of incompetence on our part and their part and corruption perhaps on their part and perhaps on our part.

I have not been able to sort it out, but someday we are going to sort that $20 billion or the $12 billion that was expended, and we

are going to find out exactly where it went. I think there are a lot of questions to be answered, but this is not the time to get into that.

One thing about that is I come from California. I have always known Mexico is going to be our neighbor no matter what happens. They will always be our neighbor, and it is better to have a neighbor that is prosperous and doing well. I supported NAFTA because of that.

Let me just say in retrospect that it seems to me that I believed in Salinas, and now I believe I got taken. It seems to me that that regime was much more corrupt and that Mexico was much more enveloped in evil, and I say that word not loosely, than what I ever believed to be possible.

Finally, let me just say this, and let me ask you this. In order to have Chile brought into NAFTA, are we going to have to have a fast track? Will there have to be a motion for a fast track type of operation here in the House for that to be successful?

Mr. SHAPIRO. We have had useful discussions with Chile and with our NAFTA partners since starting the process in June, but to really bring the negotiations to a head and to finish it I believe we will need fast track. We have asked the Congress for it and are working on it.

Mr. ROHRABACHER. Let me just say this about fast track authority. I think that free trade with Chile would probably be beneficial to us. I think that trade with Mexico, whether opening up trade, and if NAFTA has done that it would be a positive thing because we need to trade with them and permit them to work their way out of their morass down there.

The last time we gave authority to this Administration for fast track was with GATT. I will just put everyone on notice right now that although I am pre-inclined to support including Chile in a trading agreement, we were betrayed the last time this Administration got fast track authority.

A provision was put into GATT, and we were not permitted then to vote on it individually because it was fast tracked. That was not required by the GATT treaty. I am talking about the major change that occurred in American patent law that was just put—snuck—into GATT via the fast track authority. It was a betrayal of all of us who voted for fast track.

I voted for fast track. I supported NAFTA. I am somewhat of a free trader. I felt personally betrayed, and I will work against any fast track authority to this Administration after that kind of betrayal. The changes in GATT that were put in there for our patent laws undermined America's patent strength and just changed the rules of the game. It was not required by GATT.

I have made my point. If you would like to comment on it, please feel free.

Mr. SHAPIRO. I would like to comment on it, Congressman.

I know how strongly you feel about the patent issue. You have waged a very strong and eloquent campaign on this issue and have worked hard on it.

Where I would take issue with you is the charge of any kind of betrayal and misuse of the fast track process. The change in the patent law that we advocated and the change in the patent law

that was made was done through consultation with the House and Senate Judiciary Committees as we do all of our fast track work.

We do not come up with the implementing legislation on our own. We deal with the relevant committees, and those committees, the Subcommittee on Patents and Copyrights in the House and the Senate, were fully aware of what was being done and fully supportive of it.

If they did not accommodate your concerns in a way that was adequate to you, that is a problem internally with the congressional process. We have always tried on fast track to deal with the committees.

Mr. ROHRABACHER. If I could just give you a retort to that?

Mr. SHAPIRO. Sure.

Mr. ROHRABACHER. When someone votes for fast track in this body, in the House of Representatives, we are not giving up our power and our authority, our rights as elected officials, to the committees. What we have said is we are making an agreement to give up certain rights.

In a fast track authority we give up certain rights as Members of Congress so that you can negotiate. We are not saying then you can go ahead and under the agreement that nothing will be in the final agreement that is not required by GATT. That is the agreement you have.

The bottom line is I do not care what you did with the committees. You made an agreement with me as a Member of Congress that if I voted for fast track, in the end the only thing in that bill would be required by that treaty. It was not.

Mr. SHAPIRO. Congressman, I understand that fast track is controversial, and one reason is it tends to get blamed for mostly anything that people are opposed to.

The precise terms that fast track represented was an agreement that we would legislate those changes of law necessary or appropriate to carrying out the trade agreement. When we go to the committees and work closely with them, it is because they jealously guard their prerogatives as to what is necessary or appropriate.

When we said to the committee we think this change in patent law, which people have been thinking about and working on for a long time, is appropriate and we would like to make it in the implementing legislation, they supported it. We did not breach the trust that you put in us. We simply had a position that you did not agree with.

Mr. ROHRABACHER. It was wonderful that you thought it was a good provision. It would have been even more wonderful if this Congress would have been permitted to vote on this provision, which some people thought was a very good change in law, but to vote on it independently rather than have it thrown in our face saying you are going to have to vote for this change in the patent law, or you are going to have to vote against the entire world trading system. It was not fair, and that is why I will be opposed to it.

Thank you very much, Mr. Chairman.

Mr. BURTON. Thank you, Dana.

Mr. Engel.

Mr. ENGEL. Thank you. I am wondering if anyone would care to expand, and I know you have touched on it, on the status of the negotiations to expand NAFTA to include Chile and any possible timeframe for completing these negotiations?

Mr. SHAPIRO. Mr. Engel, we started the negotiations seriously in June when Ambassador Kantor, the Canadian and the Mexican Trade Ministers met with the Chilean Minister. We had talks from July 25 to August 2 in Mexico City and reviewed the whole NAFTA as it applied to Chile.

We have subsequently had a series of meetings, including one in late September, where Chile put forward a number of negotiating proposals. We are making progress, but, as I indicated, I think the time table very much depends on when the negotiations can intensify and get serious, which in turn depends on the fast track authority.

Mr. ENGEL. What do you see as the downside of the United States expanding NAFTA to include Chile? Do you see any downside on that?

Mr. SHAPIRO. I would say that I see no downside in the sense that I think the overall benefits both of including Chile and what it says to Latin America are very positive.

That does not mean that there are not individual sectors that are quite sensitive and something that we need to work out in terms of our negotiating strategy, whether it is a California wine sector worried about Chilean competition or fruits and vegetables.

These are problems we have to deal with and try to work out the best negotiation we can, but overall I believe there will be great benefit.

Mr. ENGEL. I did not support NAFTA. I voted against it with Mexico, and I did primarily because I was very concerned about the labor and environmental standards, those standards that turned out to be difficult to deal with with respect to Mexico.

How will those issues be dealt with in relation to Chile? Are you encountering much of the same, or are the circumstances different? Could you elaborate?

Mr. SHAPIRO. Mr. Engel, and again this depends to some extent on negotiating authority, but Chile has said that they would sign on to the NAFTA side agreements with respect to labor and the environment.

I think that in my view, the hard fight with respect to those issues is one that we had already in setting up the labor and environment commissions and getting some congressional support for that concept. I think those commissions are working well, and we are getting a considerable benefit from some of the labor and environment cooperation.

There is a tendency, of course, to focus on the sanctions provisions and the possibility that they could somehow come into effect without recognizing the real benefits that you can have constantly from the cooperative provisions.

Mr. ENGEL. The concern also, of course, involves potential loss of jobs and other labor issues. Have you had discussions with labor in the United States on these issues?

They obviously were very vehemently opposed to the original NAFTA agreement with Mexico. Have there been discussions be-

tween the Administration to alleviate some of the fears, which I think are very legitimate, some of the questions, for instance, that Ross Perot raises with regard to job loss in the United States?

Mr. SHAPIRO. I think, Mr. Engel, it would be fair to say that we have been speaking with representatives of labor. They have been actively involved in our advisory committee process.

I would not in any way term them to be enthusiastic about this, but I do not believe that they have the same intensity of concern that they brought to NAFTA. I do think they have a high regard for what Chile has accomplished and the importance and recognize those accomplishments.

Mr. ENGEL. In July, I had the opportunity to travel to Chile, Argentina and Brazil on a codel led by Congressman Kolbe. Congresswoman Dunn was also on that codel.

I was the only person on the codel that had voted against NAFTA. Therefore, I was left to give the other side of the story to a lot of officials, particularly the Chilean officials who were lobbying us very, very hard for expansion of NAFTA.

What are the differences between the Chilean economy today, in your opinion, and the Mexican economy in 1993?

Mr. SHAPIRO. Do you want to speak to that?

Mr. ENGEL. Anybody who would care to.

Mr. BARREDA. Congressman, I think the main differences are, first, the current account deficit of Mexico. Mexico had a much larger current account deficit. In fact, Chile is predicted to run a surplus this year.

Second, I would say the Chilean savings rate, which is extraordinarily high and pays a very high investment rate rather than depending on foreign inflows to cover the gap.

Mr. ENGEL. Would you agree, Ambassador Watson?

Mr. WATSON. Yes, Mr. Engel, and I would just point out also that Chile has had about 9 years of very rapid economic growth, about 6 percent or even higher a year, whereas Mexico for the last few years has had a much lower like 2 percent growth per year. The Chilean growth rate, as well as its internal savings rate, has been better.

Mr. ENGEL. Those were the two things that they touted to us, as you could imagine, when we were there.

Thank you very much.

Mr. BURTON. Thank you, Mr. Engel.

Mr. Wynn.

Mr. WYNN. Thank you, Mr. Chairman.

Actually, my line of thinking is quite similar to my colleague from New York. I also voted against NAFTA, but I had an opportunity to attend a conference in Miami last year, a followup to the Conference of the Americas, which seemed to indicate that Chile actually may have been a better candidate for a free trade agreement than Mexico.

I am encouraged by the information I received, but I would like to ask a couple of related questions. If you have covered them, let me apologize. I had to be out of the committee room.

If you heard the testimony, and I believe you did, of Congresswoman Kaptur, she did a very detailed analysis of job losses as a

result of NAFTA. My question in the simplified form would be why would this same pattern not hold true with respect to Chile?

Notwithstanding Chile's better economy, it almost seems in some way the situation might worsen and that Chile might be stronger from an export standpoint, but that would not necessarily help the United States.

Can you refute her statistics about the declining trade balance or certainly distinguish Chile from Mexico in terms of that issue?

Mr. SHAPIRO. Mr. Wynn, I guess I would start by saying that I do not agree with Ms. Kaptur's analysis for a variety of reasons. I tried to get into it a little bit earlier.

To give an example of one of the reasons, she focuses understandably on the automobile sector. I have done some work in that sector as well. There was an upsurge, for instance, in parts imports from Mexico in the last year or two. That upsurge had to do with a very strong demand in the United States because we were manufacturing so many automobiles. At the same time, we saw a growth of auto manufacturing in the United States and a growth of auto parts manufacturing in the United States.

For instance, from 1990 to 1994, our auto parts production in the United States rose $72 billion from $157 billion to $229 billion. To simply look at it and say we are importing more parts from Mexico I do not think is a very effective argument. It does not reflect the fact that we had virtually a record year in auto manufacturing and auto parts sales.

Mr. WYNN. What about the job losses she cited? She cited several industries with significant job losses that I believe to be correct. What is your response on that?

Mr. SHAPIRO. I guess the response varies. I do not dispute some of the ones that she cited, but there are a couple of things at work.

Number 1, a number of times you will see companies that have moved certain jobs to Mexico, and yet have done so to integrate their operations so that you can actually find cases, and GE is one of them, where you have more jobs in Mexico supporting more jobs in the United States.

Part of what NAFTA has been about is not, as Mr. Hunter said, to build surpluses here to make up for deficits elsewhere. It is to make our manufacturing capabilities and our economic capabilities in North America more competitive.

I have pointed out that our unemployment rate nationally has gone down from more than 7 percent to 5.6 percent and that for the first time in many years we have seen an increase in total manufacturing jobs in the country. Those manufacturing jobs and that increase reflects the fact that we are exporting more and that we are more competitive.

Mr. WYNN. If I could just interject for a moment? I appreciate what you said. If you would give me or submit at some later point in time a more detailed response to Ms. Kaptur's analysis, I would appreciate it.

Let me ask a couple of questions before my time runs out. What is the effect of the devaluation of the peso on Mexico's ability to import?

Mr. BARREDA. Well, the devaluation does change the relative prices between U.S. and Mexican products. U.S. products will be

more expensive. Also, we do expect that growth will return to the Mexican economy and again, thanks to NAFTA, we are going to share in that growth.

Mr. WYNN. But is it not true that as a result of basically this collapse in the Mexican economy that there is a little leeriness in the markets about investing in Mexico?

Mr. BARREDA. That is certainly correct, and that is why growth is down this year. Again, most people feel that, thanks to the measures Mexico has taken, growth will return in 1996.

Mr. WYNN. One quick question because my time is running out.

My colleague, Mr. Engel, cited the environmental concerns and the labor concerns, which I share, and you talked about side agreements. One of my objections to NAFTA was that we were taking an agreement essentially negotiated by President Bush and trying to accept that and then improve it with side agreements.

If we were to look at Chile, would we be looking at side agreements, or would we be looking at putting those issues in the agreement itself?

Mr. SHAPIRO. Well, we are still in the midst of negotiating with Chile, but part of what we have envisioned was asking the Chileans to accede to the side agreements, as well as to the main NAFTA.

Mr. WYNN. As side agreements or as part of a new NAFTA? I am assuming this is a new NAFTA we are talking about.

Mr. SHAPIRO. It is still envisioned that it would be part of the supplemental agreements.

Mr. ENGEL. I am wondering if my colleague would just yield to me for a minute?

Mr. WYNN. I would be happy to yield.

Mr. ENGEL. I think he hit the nail right on the head with the side agreements. Many of us do not understand why there needs to be side agreements and why these agreements could not be incorporated into the legislation.

We worry, for instance, about the funding. Congress is in a budget cutting mood. We worry if there is any funding that is needed for the side agreements. The new majority can simply withhold the funds for it.

There are very important concerns that we have, and we would feel a lot better if these environmental and other issues were in the main agreement and not side agreements.

Mr. WYNN. I thank my colleague.

Mr. SHAPIRO. We are, as you know, committed to the side agreements and to Chile's participation in them. Obviously we want to put the commissions on the kind of footing that they need to be on so that we do not have to worry about it and so we can work with the Hill on both sides with respect to this. Obviously there are some differences of opinion.

There was just one point Mr. Wynn made that I wanted to respond to. Considering the radical change in the currencies and the very deep recession that Mexico is in, our exports have actually held up much better than one would have expected.

Any decrease is unwelcome, but our exports are down 9.1 percent to Mexico this year as opposed to 1994, which was a good year. In August, they were down 5 percent from the previous August, which

suggests to me, No. 1, that we are still exporting a lot there, and these are very competitive products. No. 2, we still have a preferred trading position there.

Mr. BURTON. However, we still face a $20 billion trade deficit this year, which is very bad for our economy. It does not look like it is going to get any better any time soon.

The other thing I would like to ask you is if Chile comes into the NAFTA agreement, will it have a member on a four-part board to settle trade disputes like the tribunal? Is that one of the elements that is going to be incorporated into a trade agreement with Chile?

Mr. SHAPIRO. That is one of the things that is under discussion at this time, Congressman.

Mr. BURTON. It would appear to me that if there is going to be real fairness that you are going to have to incorporate one Chilean along with a Mexican, a Canadian and an American in some kind of a decisionmaking process.

Once again, that is very disconcerting to me because we may have an American company that feels like it is being mistreated by this group, and it will have no recourse in American courts. I hope that down the road you will take a hard look at that.

With that I want to thank the panel very much. You have been very, very helpful.

Our next panel is Dr. Sidney Weintraub, who holds the William E. Simon Chair in Political Economics at the Center for Strategic and International Studies; and Kevin Kearns, president of the U.S. Business and Industrial Council.

Dr. Weintraub and Mr. Kearns, I really want to thank you very much for your patience. It is always tough being on the third panel when there are so many questions being asked of previous panels.

Many of my colleagues have left, but let me just assure you that both of your statements and the questions and answers that you are going to be giving will be conveyed to all of my colleagues on the Floor when we get into a debate on Chile and further NAFTA expansion.

With that, let me start with you, Dr. Weintraub.

STATEMENT OF DR. SIDNEY WEINTRAUB, WILLIAM E. SIMON CHAIR IN POLITICAL ECONOMICS, CENTER FOR STRATEGIC AND INTERNATIONAL STUDIES

Dr. WEINTRAUB. Thank you, Mr. Chairman. You have my statement and, therefore, I will be very brief. There is no reason to read all of it.

Let me start out by saying that I supported NAFTA, and I still do. I also support the accession of Chile, and I also believe that we ought to in due course negotiate our way toward a hemisphere-wide free trade area. Those are the bases with which I start, and my statement follows from that.

Let me make ten points. I will make them briefly without very much elaboration and then be prepared to elaborate in any question and answer session.

My first point, one that I think was made by other panelists before, is that we capture more of the market in the Americas than we do in any other region of the world. On average, our share is about 40 percent of the hemisphere market, and on average the

other big markets where the United States sells like Asia and Europe it is closer to 20 percent or even less.

What that means is that economic growth in this hemisphere benefits our exporters more than growth in any other hemisphere. This hemisphere already takes 40 percent of U.S. exports, which is more than the Asian market and much more than the European market. I am including Canada in this as well.

Second, on free trade issues, the average U.S. tariff is about 3.5 percent. It is quite low. For most commodities, it is irrelevant. There are exceptions. The average tariff in Latin America runs at least three times that, and they also have peaks. Therefore, if we negotiate the mutual reciprocal elimination of tariff barriers, they have to come down more than we do. That, too, is a point that is worth keeping in mind.

Third, the reason we enter into regional agreements such as NAFTA and with other Latin American countries is that we are able to make more progress more quickly than we make in the multilateral negotiations.

U.S. agricultural exports to Mexico were opened much more widely in NAFTA than they had been earlier. The progress made on intellectual property issues in NAFTA, on trade in services, national treatment for U.S. investors, all of those, were pioneered in NAFTA, and some of them were subsequently picked up in the Uruguay Round.

Regionalism cannot replace the multilateral structure, but it can stimulate progress in the multilateral structure.

Fourth, one of the ways that most industrial countries promote competitiveness of particular industries is to go into production sharing within their regions. Japan does it quite extensively in the Asian region. The Europeans do it in eastern Europe and elsewhere. We do it extensively in Canada, Mexico and the Caribbean.

To preclude our companies from competing on this basis in the way that everybody else in the world competes would stifle the competitive nature of many of our companies.

That is one of the major areas of importance for NAFTA, this kind of production sharing with places that are reasonably close and where the transportation costs are possible. If we did not do it in our own region, we would do it anyhow because that is the nature of the world, but it would be more expensive.

Fifth, I do not think NAFTA had anything to do with Mexico's problems. I think Mexico's problems were of their own internal mistakes. I think they created their own bed, and they are, unfortunately, having to lie in that bed.

NAFTA is operating the way it should. When things were going well last year, our exports boomed. They are going badly this year, and our exports are coming down.

Two points I think are worth keeping in mind. One, Mexico this year will still be our third largest market, despite the economic decline. Two, when Mexicans had to correct the economic problems, and they are in the process of doing this, they did not put on import restrictions against products from the United States. In previous financial crises in 1982 and before, that is exactly what they did. NAFTA made a difference in that.

Sixth, I think that the financial rescue package for Mexico is working. The peso is stable. Interest rates are coming down. Inflation is now less than 2 percent a month. Had Mexico defaulted on its Government obligations, this would not be the case today. Yes, we put U.S. money at risk, and we are collecting interest on that money. I think the alternative would have been much worse.

The economic situation in Mexico, the real economy, is not in good shape. I was talking about the financial situation. Unemployment has risen by about 1,000,000 or 1,500,000 people this year. There are a lot of bankruptcies of small companies. The economic price that Mexican workers and businesses are paying for the mistakes of the country is enormous.

This is the biggest economic catastrophe that Mexico has faced since the end of the Revolution and Civil War. They are dealing with it, though, and I think that is the important issue. All the evidence is that Mexico will probably come out of the economic depression by next year.

Seventh, I think Chile is the ideal country to be the first new adherent. It has a low uniform tariff. It is 11 percent. It is a true democracy. Chile has now had two Presidential open elections since General Pinochet resigned. Their GDP growth this year is about 7 percent. They have been growing regularly. They do not have too many restrictions. I think in a sense we could not pick a more ideal country for the negotiation.

Eighth, I guess I am deeply disappointed at the U.S. Government and the U.S. Congress. There was tremendous excitement throughout the hemisphere when President Bush proposed the idea of a free trade area from Alaska to Tierra del Fuego. We have done nothing since then except call some meetings and make a bunch of speeches.

We have promised Chile through two presidents that we would move ahead. We have not been doing it. Instead of showing leadership, we are lagging behind in doing things. This does not, in my view, speak well of a great power where support has come from two presidents of different parties.

Meanwhile, and this is my ninth point, the European Union, unlike us, is expanding all of its trade links. They are even opening negotiations with MERCOSUR. They are showing leadership. We are not.

Finally, let me make a political point, but it is mixed with economics. This is our hemisphere. It is our hemisphere because of where we are, and it has been our hemisphere from the very creation of this democracy, of this republic. If we cannot show leadership here, I fear that we cannot show it any place.

Thank you.

[The prepared statement of Dr. Weintraub appears in the appendix.]

Mr. BURTON. Thank you, Dr. Weintraub.

Mr. Kearns.

STATEMENT OF KEVIN KEARNS, PRESIDENT, U.S. BUSINESS AND INDUSTRIAL COUNCIL

Mr. KEARNS. Thank you, Mr. Chairman. I compliment you on holding this hearing.

I represent the U.S. Business and Industrial Council. We were opposed to NAFTA, and we were opposed to the creation of the World Trade Organization through the GATT Round. It surprises many people that a business organization would be opposed.

There is a distinction to draw between small- and medium-sized businesses in this country and American multi-national corporations. Small- and medium-sized businessmen feel that these days the American economy is being run for the benefit of American multi-national corporations, their executives and their shareholders and not with an eye to average American workers and average American companies as it were.

Two-thirds of all the job creation in this country in the last 20 years has been in the small business sector. The Fortune 500 have not created a single net new job in the United States in spite of increased exports in over 20 years.

The reason is simple. They are downsizing to in essence respond to Asian competition. They are moving their capital and technology around the world chasing cheap labor. They are closing factories in the United States.

What is happening to the average American worker is that wages and productivity have been delinked. His and her standard of living is being lowered. They are tumbling down the wage and job scale into lesser jobs, into the service industry.

In 1950, one in three Americans worked in manufacturing. Today the number is one in seven. The service industry has gone the opposite direction. Now, I am not against service jobs. I am glad that there are jobs for Americans. On the other hand, service jobs generally pay significantly less than manufacturing jobs.

There is a real difference in perspective among the multi-national corporations, their executives, their lobbyists in Washington and small- and mid-sized business.

The businessmen I represent generally employ about 100 to 200 people. They are involved in the manufacturing industry. They live in the same town as their employees. When they walk the assembly line, they know who those employees are. They do not lay off 4,000 people at a clip without ever having seen their faces or known their names.

They are intimately involved in these communities, and they see what is happening in these communities with global competition, with downward pressure from foreign labor markets on U.S. wages.

They realize that with the demise of the Soviet system, the opening of China, the opening of India, etc., there are about 4,000,000,000 of the world's population who formerly were not involved in international trade who now are involved. Many of those people, the adults and the children in fact in many of these countries, are selling their labor on the world market. American workers are competing against that labor.

This is the big picture. This is what NAFTA allegedly was going to help Americans compete against, all these countries that have come on line around the world, especially the Asian countries where U.S. goods are still blocked from getting into Japan, getting into China, etc. Then we were going to go to Mexico, and somehow that was going to make things right, as Congressman Hunter said, competing with the Asian tigers.

Well, the other claim, of course, that was made here several times today was we should somehow feel good that our jobs went to Mexico instead of Singapore. You know, the jobs may have gone somewhere else anyway.

The answer to that is the person who has lost a job does not feel great that it went to Mexico versus Singapore. This is an indication that our overall trade policy is a failure. Americans are earning less income in terms of real wages. Their jobs are disappearing.

With your permission, I would like to put two articles into the record, one from the New York Times and one from the Wall Street Journal. It is just three pages, Mr. Chairman.

Mr. BURTON. Without objection.

Mr. KEARNS. August 28, 1995, New York Times, an article by Keith Bradsher, "Skilled Workers Watch Their Jobs Migrate Overseas," a blow to the middle class. College educated foreigners are doing high technology tasks for far less pay.

It goes on to illustrate how American corporations are moving increasingly higher paying jobs overseas. Software engineers from Silicon Valley are losing their jobs to software engineers in Bangalore, India. Banks and insurance companies are moving their processing operations to Asia.

The article from the Wall Street Journal is headlined, "Will Flat Wages Beget Future Trouble?" I would just like to quote, "The trends are so strong...", that is, a delinkage between productivity and real compensation, "...that some Wall Streeters have begun to sound like radicals. Steven Roach, chief economist at Morgan Stanley & Company, an institution not known for harboring subversives, warns of a backlash unless workers begin to receive a just reward for their productivity contributions."

What is happening I think is what Ms. Kaptur said. The global competition is putting extreme downward pressure on wages of all sectors in the American economy, not just the blue collar sectors. With increasing trade liberalization has come an increasing gap between productivity and wages.

Let me turn for a minute to some of the other claims that were made at the hearing and this idea that the devaluation in Mexico of the peso was not related to NAFTA. Of course it was related to NAFTA.

Various Members of Congress here have said and the witnesses have said that this was just bad policy on the part of the Mexican government. Let's go a step further. Why did the Mexican government have this bad policy? Why did Salinas undertake these policies?

He created a bubble economy. He created an illusion or tried to create the illusion that Mexico was a stable, first-world country that was taking in U.S. exports. What happened, of course, was that the market has been constantly devaluing the Mexican peso over the past number of years. During this period, Mexico used all its foreign exchange to prop up the value of the peso. Mexico did not devalue the peso. The market devalued the peso.

This Mexican government under Salinas' leadership was able to create this illusion. Why? Because they wanted to get NAFTA.

Several people have said well, you know, it is not so bad because our exports are only down 9 percent in the wake of this NAFTA-

related peso crisis. Well, of course Mexico has not imposed the same controls it did in 1982 because the only way out of this crisis for Mexico is to earn some more foreign exchange.

How are they earning foreign exchange? Let's take a look at their imports from the United States. Very few of them stay in Mexico as consumer goods and reach the consumer market. It is even harder now because purchasing power of Mexicans has fallen about 20 to 30 percent with this devaluation.

About 25 percent of them are capital goods, U.S. factories moving down there or Mexican factories buying capital goods which are in place in Mexico to compete against U.S. firms to send products back to the United States. The remainder are intermediate goods, goods that are assembled in Mexico to go back to the United States.

Of course they are not going to cut off that source of foreign income. They need that income to deal with the overall crisis. They are going to export their way out of this crisis, the exports going to the United States.

Mexico is still in deficit with its other major trading partners. Remember we heard during the NAFTA debate that Mexico was going to be an export platform? U.S. companies would move down there and compete in world markets. That has not proven the case. We are not competing in world markets through Mexico. The goods are coming back here.

I also would recommend that people look at the European experience and the European model. When Portugal and Greece were integrated into the EC, no one lied to the European people and said this is going to be easy when you have these two disparate types of economies.

You have an advanced economy like Germany's and a backward economy like Portugal's. There were billions and billions of dollars of subsidies paid over many years to get these economies ready to be integrated.

Somehow with an economy 4 percent the size of ours in Mexico, we were going to do it overnight without any trouble. This was part of the illusion that the NAFTA proponents created.

Look at West Germany and East Germany when they tried to unite. The billions of deutsche marks that the west had to spend to bring East Germany and integrate it into their economy almost caused the fall of the government. It created serious financial problems for both Germanies.

Not only is there a problem now, but there are going to be problems in the future integrating this very backward economy, this very corrupt country. Let's not forget that the DEA estimates that 75 percent of the illegal drugs coming into the United States are coming from Mexico. Let's not forget that the former President's family is involved or reputed to be involved in assassination of high-level figures.

Let's not forget that many Mexican Army officers or at least some Mexican Army officers are thought to be in the drug trade. Let's not forget that illegal immigration has increased since NAFTA. Of course, as has been pointed out, our trade deficit has skyrocketed.

I know I am taking perhaps more time than I should. I would just like to spend a minute on Chile because I just spent a week down there at the invitation of CONUPIA, which is their small- and medium-sized business federation. The small and medium size sector in Chile employs about 80 percent of the country's population.

There are four main goals of the various Chileans, and I talked to many different people from all walks of life in Chile. There are four different goals from the Chilean perspective for NAFTA, and that is increased access to a broader market, increased foreign investment, more intense competition in the home market, a favorite of free traders, and prestige in being linked to the United States.

I think all of these things are going to happen if Chile joins NAFTA, but I think there are going to be a lot of unintended consequences because both on the American side and on the Chilean side, their accession has not been subject to rigorous analysis.

The small businessmen in Chile tell me that they cannot compete. They are 20 years behind in terms of technology, management techniques and access to capital. What is going to happen if the Chilean market opens, and maybe as Americans we should not be worrying about this, but I think on the political side we do have to worry about. It is going to produce significant unemployment.

The factories in Mexico, the multi-national companies there, they are not going to relocate in Chile. It is a small market, 15,000,000 people. They are going to send goods down to Chile, which is going to knock out a large part of their manufacturing sector.

Now, great. That is liberalization. That is rationalization. You have political problems with a whole bunch of unemployed people who formerly worked in a manufacturing sector.

[The prepared statement of Mr. Kearns appears in the appendix.]

Mr. BURTON. Let me ask you a couple of questions.

Mr. KEARNS. Sure.

Mr. BURTON. Do you think that we should negotiate our trade agreements on a bilateral basis rather than on a multi-lateral basis?

Mr. KEARNS. Absolutely, Mr. Chairman. I heard your earlier remark on this, and I think that is exactly the case here.

We have five or six goals, the United States does, aside from this goal of grabbing all of Latin America for ourselves, but specific goals in the case of there is a lot of software piracy in Chile. There is a tax that tends to discriminate against American automobiles. Our poultry and our fruits cannot get in there. Our pharmaceuticals are discriminated against because of sections of the Chilean patent law, and our whiskeys are discriminated against with a tax.

These types of things, plus the 11-percent tariff, can be easily addressed in a bilateral negotiation.

Mr. BURTON. But in a multilateral agreement you have all kinds of problems.

Dr. Weintraub.

Dr. WEINTRAUB. I cannot answer your question as a one-handed economist, one way or the other. We have to do both.

Certain agreements I think are better negotiated bilaterally or regionally because we can reach deeper commitments. Certain

other themes that are worldwide in nature we are best off negotiating them multilaterally.

If you want to get trade in services globally, and the United States is very competitive in this area, you want to go multilateral. Subsidy arrangements are best dealt with multilaterally. I think that using the two methods together is much more powerful than choosing any one of the two alone.

Let me make one other point.

Mr. BURTON. I used to be in a partnership with three other people. Inevitably when we had a disagreement, two of three would get on one side, and one would be on the other. It was unavoidable, and we were all gentlemen. We were partners. The next day we would have another problem, and you would have two on the one side and one on the other side. It was a constant problem that we dealt with because our profit and loss statement was dependent upon us working things out. We did.

When you get multiple countries, does that not put one country inevitably in a position where they are at a real disadvantage at some point?

In a bilateral case you only have the two that have to sit down and negotiate hard core over a conference table.

Dr. WEINTRAUB. The reason the Uruguay Round took six or 7 years is because there are these kinds of problems that have to be dealt with.

Mr. BURTON. And the problems remain in many cases.

Dr. WEINTRAUB. Well, some remain, and some were removed. We have reached better subsidy arrangements than we ever had before. We have new rules on agriculture that we never had before.

Mr. KEARNS. But in the interpretation of——

Mr. BURTON. Let Dr. Weintraub finish.

Dr. WEINTRAUB. Let me finish. We do operate in the entire world, not just bilaterally. Therefore, the progress we have made since the end of World War II, if you believe in liberal trade, was made primarily in the multilateral framework.

I believe you have these problems, and I accept that. Therefore, it is quite clear to me that when you negotiate on a regional basis you can make more progress more quickly and more rapidly. That then becomes a stimulus to the progress on a global basis.

Mr. BURTON. Did you hear my argument that I raised? In the case of NAFTA, the tribunal would be deciding various trade disputes and many times imposing a penalty on a company that might be viewed to be in violation of NAFTA. There is no appeals process within U.S. Courts. Do you think there is a constitutional problem with that?

Dr. WEINTRAUB. No, I do not.

Mr. BURTON. Why is that?

Dr. WEINTRAUB. Let me alter your premise here. You assume that when there is a trade dispute between two countries, a vote gets taken by all four. The tribunals are set up by panelists from the two countries in the dispute, not by all four. It is not decided by a vote of countries.

Mr. BURTON. What about an individual company in the country that is viewed to have violated the NAFTA agreement and there is a penalty imposed by the international tribunal?

Dr. WEINTRAUB. The international tribunal does not impose a penalty. That is not the way these things work. These disputes become bilateral disputes then, not necessarily multilateral disputes, even though there are four countries that are members.

In the overall management of an agreement that has four members, you may have four countries all voting on it or all reacting to it, but it is highly unlikely that these things would be done by votes. That has never been the history of the GATT, and it is unlikely that it is the history of the World Trade Organization.

Mr. BURTON. Mr. Kearns, would you like to comment?

Mr. KEARNS. I think that we have seen since the inauguration of NAFTA and going back to the Canadian-U.S. Free Trade Agreement, the precursor of NAFTA, as well as what has happened with the World Trade Organization since that came into being, that the theory is simply that free trade rules will be applied uniformly.

There is some sort of magic to economic rules. They are kind of like chemistry, you know. You put a couple of atoms together in a test tube, and they interact in a standard way.

That is not what happens. In fact, the decisions of dispute resolution panels are highly political and are going to remain so. They are not going to simply apply some free trade rule or tariff standard or whatever it might be to the offending country. This is about getting a bigger piece of the pie for your companies and your country.

I think you have a very valid concern. We have seen this process politicized already, especially in the case of the Canadians. We have seen Mr. Ruggiero, the head of the World Trade Organization, play politics already.

I think this is a serious concern, and I share your concern about the sovereignty and the constitutional issues, too.

Mr. BURTON. Let me ask you this——

Dr. WEINTRAUB. Let me make one comment because he is a mass of misinformation, and I want to touch only on one little element of it.

Mr. KEARNS. Why do you not talk about the Canadian lumber panel?

Dr. WEINTRAUB. I can if you want, but let me talk about what I want to talk about.

There have been two recent Mexican steel cases where they imposed anti-dumping duties that were brought before the Chapter 19 panel. The Mexican panelists threw them out.

Mr. BURTON. That was mentioned earlier today.

Dr. WEINTRAUB. Except for that one case of the extraordinary challenge where the judges were divided by country, we have not had that typically in these panels.

Mr. BURTON. There was an advertisement that was in a U.S. business magazine. It had a businessman looking pensively out the window, and he was saying, "I cannot find any place in the world where I can get labor, wages and fringe benefits for $1 an hour." Below it in big, bold type was the conception, "Yes, you can in the Yucatan."

The implication was that for $1 an hour you could get wages and fringe benefits for a manufacturing, labor-intensive industry if you

located down in the Yucatan. That is one problem that you face because of the huge disparity in wage rates.

The second thing is that with NAFTA you have the import tariffs coming down in many cases over 15 years on the Mexican side while they come down over 5 years on the U.S. side.

If an American company is labor-intensive making microwave ovens, and they know that if they go down to Mexico they can have access to both markets and can also take advantage of very, very low wage rates and fringe benefits in this labor intensive industry, what is the inducement for the company to stay in the United States?

Mexico has lower wage rates, lower fringe benefit rates, and U.S. companies that relocate can drive their competitor right out the window unless they also decide to relocate in Mexico where they have the same advantages.

Dr. WEINTRAUB. Two or three comments. One, I do not think you can equate wage rates with productivity. Therefore, you cannot assume that a place where the wage rates are lower is necessarily going to be cheaper in the final outcome.

Mr. BURTON. Dr. Weintraub, I used to work at RCA. When the red light came on, I took the red television chassis off the red hook and put it on a red cart and took it to a red spot. There are a lot of assembly line production companies that do the same thing. They teach their people to put the same screw in the same hole all day long. Those are labor-intensive industries.

Dr. WEINTRAUB. Those industries will move, yes.

Mr. BURTON. That is right, but how do you protect U.S. jobs? I am not a protectionist. I am for free trade if we can make sure we can work it out fairly. How do you protect the job loss over a long period of time from taking place with those kinds of disparities?

Dr. WEINTRAUB. We are going to lose some jobs because of changing conditions both internationally and within the United States.

We lose a lot more jobs because of changing conditions within the United States than we do from the 10 percent of our GDP that is exported. In other words, we do have to adapt to changing conditions.

Your comment also that most Mexican tariffs will go down over 15 years is not quite accurate. Most of them will go down——

Mr. BURTON. Not most, but many.

Dr. WEINTRAUB. Mainly the sensitive agricultural products are the ones where tariff reductions will be delayed for 15 years; corn, which is their staple is the best example. Those are the ones that are being delayed out to 15 years. Most of the others are going to go down over 10 years. Remember, they started three times higher than we did, so——

Mr. BURTON. Our trade barriers come down over 5 years primarily. Even if there is a 10-year lowering period, that still gives Mexico a 5-year distinct advantage.

Dr. WEINTRAUB. Our tariffs for the most part in trade with Mexico, on imports from Mexico, tend to be irrelevant, Mr. Chairman. There are exceptions to that obviously. I do not want to generalize. They are low to start with.

Mexican devaluation of the peso has been close to 50 percent, and our import tariffs are 3 percent. What difference does a tariff make in these circumstances?

Let me make one other comment about the Chilean level of the same tariff, and then I will stop.

Mr. BURTON. Sure.

Dr. WEINTRAUB. I want to talk as an economist now. Chile has a uniform tariff. That makes a great, big difference. It means they are not trying to pick and choose as to which industry they want to subsidize and which one they want to protect.

If you have a uniform tariff of 11 percent, that is almost the equivalent of a zero tariff. The difference will show up in the exchange rate. Therefore, I cannot understand the argument of Chilean small business groups that they want to maintain that 11-percent tariff because that protects them. It is not protecting them.

Mr. BURTON. I will be glad to let Mr. Kearns comment on that.

I do not think many of us in Congress have near the hesitation with Chile that you might think, if we could work out a bilateral trade agreement because many of us believe in free trade. We also think it should be fair. That is why a bilateral approach makes more sense to me.

Mr. Kearns.

Mr. KEARNS. Let's go back to the question of the factories leaving. I think the claim is that Mexico's economy as a whole is quite unproductive. It is quite inefficient.

In fact, in the maquiladora plants in many industrial sectors, electronics and automobiles especially, there is higher productivity than there are in U.S. plants. The Ford plant in Atlanta has won awards over the years for being very productive, but the Ford plants in Mexico are more productive.

The same thing is true of Japanese electronics firms; Sony TV plants, for example. Foremen of the plants have said their plant is as productive as our plant in Alabama and our plant back in Japan.

You have to look at where our trade deficit is, the manufacturing sectors that are moving down there. They are getting excellent productivity. When you get that same or better productivity as the United States at one-tenth of the wages or at your $1 a day in the Yucatan, of course you are going to move down there.

The second thing is let's look at the devaluation in terms of tariffs. There is the question you raise about how fast tariffs are coming down on both sides and the unequal rate at which they are coming down. I agree with that.

When you devalue your currency by 43 percent, in essence we make up 10 percent because one of their tariffs comes down, but you have a 43-percent devaluation, which means the whole purchasing power has gone to hell in a hand basket.

That, in effect, replaces the tariff, and that is what the Mexican government did. They snookered us into NAFTA. They devalued. It is clear that our goods cannot get in there. There are a couple of ways you can skin that cat, you know.

Mr. BURTON. The goods may be able to get to Mexico, but Mexicans often cannot afford to buy them. That is part of the problem.

Mr. KEARNS. Yes.

Mr. BURTON. This has been a very long hearing, and you gentlemen have been very patient. I really appreciate you both waiting so patiently. If you have any final comments, I would be happy to hear them.

What I would like for you to do for the record and for the members' benefit is to submit any documentation that you would like for us to have when we get into the debate on fast track with Chile or on further negotiations that would involve NAFTA.

I would like to have both your arguments so I can distribute them to my colleagues. I guarantee that I will take a hard look at them.

Do you have any final comments?

Mr. KEARNS. I just want to go back to Chile for a second. Eighty-seven percent of Chile's exports are in its natural resources. Ninety-nine percent of the foreign direct investment is going into the natural resources of forestry, fishing, agriculture and mining.

When you apply capital and technology in greater amounts to these natural resources, you are going to get severe dislocations both among the agricultural workers, the fishermen, etc. They are going to get kicked out of their jobs by factory ships, by crop harvesters, etc.

The Chilean economy, even though it is growing, is not ready to absorb those people, plus there will be increasing pollution. Chile's rivers are already polluted by agri-toxins which have been used significantly during this period of expansion and from the runoff from the mines.

It is not the small- and medium-sized business sector which employs 80 percent of the population that is going to benefit from somehow increased foreign direct investment. I would submit that there is a significant chance with increased unemployment from the agricultural sector, from the fisheries sector, and from the small business sector that rather than stabilizing Chile, the NAFTA agreement could destabilize it through significant unemployment.

There are significant concerns I think we should look at. The free trade answer is well, the market will sort it all out. The market will value labor. The market will create new opportunities. But if there is significant unemployment in a country that small, there are going to be significant political problems as well.

Mr. BURTON. I am going to be going down there sometime this winter, and I will raise these questions with our counterparts in the Chilean government before we get to that point.

Dr. Weintraub.

Dr. WEINTRAUB. I am just going to make one brief comment.

Mr. BURTON. Thank you, sir.

Dr. WEINTRAUB. I lived in Mexico many years ago, and I have studied Mexico for many, many years. I think I have a sense of the country.

I heard in some of the earlier panels a lot of the attacks on Mexico for irregularities, corruption. Some of these are justified. I do not quarrel with that. The thought that Mexico snookered us and then deliberately brought on the deepest depression in their modern history causing a tremendously high decline in growth and

high unemployment almost boggles the mind. I just cannot understand how anybody makes that argument.

Mr. BURTON. Somewhere the truth is in between, I think.

Dr. WEINTRAUB. Yes.

Mr. BURTON. Thank you, Dr. Weintraub and Mr. Kearns. We appreciate it very much.

This meeting stands adjourned.

[Whereupon, at 1:04 p.m., the subcommittee was adjourned to reconvene at the call of the Chair.]

APPENDIX

MR. ROTH'S OPENING STATEMENT

IT IS A PLEASURE TO CO-CHAIR THIS IMPORTANT HEARING WITH MY GOOD FRIEND, CHAIRMAN BURTON OF THE WESTERN HEMISPHERE SUBCOMMITTEE.

CHILE HAS BEEN A TRUE ECONOMIC SUCCESS STORY. DUE TO REFORMS BEGUN TWENTY YEARS AGO, IT IS NOW GOING THROUGH ITS 12TH YEAR OF ECONOMIC EXPANSION.

WITH A GROWTH RATE OF OVER 6 PERCENT THE LAST TEN YEARS, CHILE HAS BEEN PERFORMING ON A PAR WITH THE MOST DYNAMIC ECONOMIES OF THE ASIAN PACIFIC RIM.

AND IT HAS BEEN DOING SO VIA ECONOMIC REFORM AND LIBERALIZATION:

- FOR THE LAST DECADE, CHILE'S MARKET-BASED ECONOMIC POLICIES HAVE PROVIDED A NEEDED BEACON OF MACROECONOMIC STABILITY IN LATIN AMERICA;
- CHILE HAS LED LATIN AMERICA'S PRIVATIZATION MOVEMENT;
- AND, IT HAS MAINTAINED A MORE OPEN TRADING SYSTEM THAN ANYONE ELSE IN LATIN AMERICA.

IT IS ALSO USEFUL TO NOTE THAT IN 1994 THE U.S. HAD A 950 MILLION DOLLAR TRADE SURPLUS WITH CHILE.

THIS IS A COUNTRY THAT WE SHOULD BE ALLIED WITH CLOSELY ECONOMICALLY. IT IS ALSO A COUNTRY THAT COULD POSSIBLY TEACH US SOME THINGS.

FOR CHILE HAS RUN A NATIONAL BUDGET SURPLUS FOR EIGHT STRAIGHT YEARS.

AND IT'S NATIONAL INVESTMENT RATE HAS HOVERED AROUND AN ASTOUNDING 27 PERCENT OR GROSS NATIONAL PRODUCT, ITS SAVINGS RATE AT AROUND AN IMPRESSIVE 24 PERCENT.

THIS IS THE KIND OF PERFORMANCE THAT WE SHOULD BE SEEKING THROUGHOUT LATIN AMERICA.

I LOOK FORWARD TO OUR WITNESSES VIEWS ON HOW WE CAN WORK WITH CHILE TO EXTEND FAIR TRADE AND ECONOMIC DISCIPLINE THROUGHOUT LATIN AMERICA.

The Honorable Jim Kolbe
October 25, 1995
House Committee on International Relations
Subcommittee on International Economic Policy and Trade
Subcommittee on Western Hemisphere

Introduction

Thank you very much for the opportunity to testify today. I want to commend Chairman Burton and the Subcommittee for holding this hearing. Given Mexico's current -- though I believe temporary -- economic problems, it is certainly appropriate to take stock of how NAFTA is working now before we take another step toward the clear mandate of the Summit of the Americas meeting last December in Miami -- hemispheric free trade. Today, I want to tell you why I believe NAFTA is working as we intended and why it is critical to the economic future of the United States to continue to pursue hemispheric free trade.

NAFTA and Mexico

It has been nearly two years since Congress passed NAFTA. However, we should remember that trade agreements are a long-term proposition. There will be short-term fluctuations which will have both positive and negative effects on U.S. interests. We would do well to remember that NAFTA is a foundation for North American trade, phased-in over 15 years. Under the terms of the agreement, many of its most critical provisions have not even begun to be implemented.

Still, it can be said that NAFTA is working. During good times, it spurs economic growth, creating jobs on both sides of the border. When an economic upheaval occurs, such as the peso devaluation, it cushions the impact domestically, limiting U.S. job losses and preserving jobs. NAFTA is indeed a "safety net" for the more than 700,000 U.S. workers whose jobs are supported by exports to Mexico.

NAFTA had a good first year. Prior to the devaluation of Mexico's peso in December, 1994, $20 billion of new trade took place between the U.S. and Mexico. That means that one-fifth of all U.S.-Mexico bilateral trade was new trade, generated in NAFTA's first year. Although U.S. exports to Mexico are down 9.6 percent so far in 1995, *they are still seven percent higher than pre-NAFTA levels.*

The best test of an agreement is how it works in bad times. What NAFTA did was lock-in Mexico's trade and economic reforms. NAFTA prevented Mexico from resorting to the standard solution of developing countries in crisis: imposing import barriers, restricting capital movements; and limiting economic activity. In fact, this was precisely Mexico's response to their last financial crisis in 1982. Then, Mexico closed its market by raising import duties to 100 percent and requiring an import licenses for virtually everything. U.S. exports were consequently cut by more than 50 percent, a blow that took our exporters six years to recover

from. Based on this experience, without NAFTA, in the wake of the peso crisis, U.S. exporters could have faced a $25 billion plunge in sales to Mexico and not fully recovered before 2000. Instead, U.S. exports to Mexico are down less than 10 percent or by approximately $5 billion. Indeed, NAFTA has provided a steadying hand for U.S.-Mexico bilateral trade. This year, when Mexico raised duties on selected products, it exempted NAFTA goods because the agreement prohibited such actions.

Some of NAFTA's critics allege that NAFTA itself caused the Mexican peso crisis. Such a claim is, frankly, preposterous. Mexico's financial crisis was caused by an overdependence on foreign capital and protracted, politically-motivated, overvaluation of the peso. In real terms, the peso had been appreciating since 1987. When a bungled devaluation, following a combination of political shocks, caused rapid capital flight, the peso went into a free fall. Moreover, NAFTA did not contribute to the soaring Mexican current account deficit. Despite the fact that $20 billion of new trade took place between the U.S. and Mexico in 1994, the U.S. trade surplus with Mexico remained virtually unchanged at $1 billion. Even taking the longer view, during 1987-1994, the years of strongest trade expansion, two-way trade flows exceeded $500 billion, yet the U.S. had run a *cumulative* trade imbalance with Mexico of less than $2 billion -- that is very, very close, given such large total trade between the two countries.

Some economists are citing the recent trade statistics as evidence that the newly-created trade deficits have led to the loss of thousands of jobs and a decline in real wages. *Wrong again!* While diminished short-term opportunities in Mexico may have led to some dislocation of workers, since NAFTA was implemented, U.S. manufacturing employment has actually increased by 225,000 jobs and total employment in all sectors has increased by 340,000 jobs. Furthermore, as already noted, NAFTA created a safety net for the 700,000-plus workers whose jobs are, and continue to be, supported by exports to Mexico. With respect to criticisms that NAFTA has brought about a reduction in U.S. wages, the average *real* U.S. manufacturing wage is 0.5 percent higher today than it was in 1993, the year before NAFTA. U.S. workers continue to compete successfully against less expensive Mexican -- or Indonesian -- or Chinese -- labor because we have higher productivity, technology and infrastructure base -- *and that gap is widening, not narrowing.*

Most forecasters project positive economic growth for Mexico in 1996, though I think that it may not occur until 1997. Regardless, when it does, the U.S. will again realize the economic benefits which we contemplated from NAFTA.

Importance of Latin America and Chile

Now, let me speak briefly about Latin America and Chile.

Testimony of the Honorable Jim Kolbe
October 25, 1995

Not moving ahead with Chile's membership in NAFTA in a timely fashion would be unfortunate for a country that has long qualified for partnership in a free trading relationship with the United States. Moreover, because of the commitments we have made to Chile, failure to move ahead would damage U.S. credibility in the hemisphere and deal a sharp setback to prospects for the hemispheric free trade contemplated by the Miami Summit.

Such a result would be a major political and economic setback for hemispheric integration. If the dream of hemispheric free trade evaporates, the U.S. risks losing as much as Latin America. Countries in Latin America already are forming overlapping regional trade alliances, such as MERCOSUR. Trade within and among these groups has grown rapidly. Latin American exports to other destinations within the region have increased nearly 100 percent in real terms since 1982. As might be expected, the relative importance of the U.S. market to Latin America has declined slightly given the growth rate of both global and regional trade. If we do not pursue hemispheric free trade in a timely way, by the time we do wake up to the need to act, Chile and other Latin American countries may have little desire, or need, to negotiate with the United States.

Chile's membership in NAFTA would be a visible acknowledgement of the dramatic way it has restructured its economy and entrenched democratic institutions. Clearly, these are prime objectives of the work of this Subcommittee, and of Congress, with respect to Latin America in the last decade.

In the early 1980s -- the midpoint of the Pinochet military regime -- Chile suffered a 90% devaluation of its currency in just 12 months, a collapse in international copper prices, and the failure of the domestic banking system. Chile went through an economic crisis more intense in relative terms than our own Great Depression.

Chile responded by decisively overhauling its economy. Sweeping deregulations and tax cuts and tax simplifications eased market entry for thousands of small and mid-sized firms, a process that rapidly broadened Chile's economic base. A low, uniform tariff was introduced. No industry was kept under a "strategic" umbrella, deserving of special protection from international competition. As might be expected, economic liberty led to demands for political reform. Political opposition to General Pinochet's autocracy was energized and eventually overturned his rule at the ballot box. Democracy is working again in Chile.

Over the past decade, Chile's gross domestic product has grown by an average of six percent a year. In the most recent three years, it posted an average annual growth rate of 7.1 percent. It has achieved an annual savings rate of 26 percent -- a rate far above most OECD countries. Chile has even privatized its Social Security system. As a result, the assets of Chile's private

pension plans are now equivalent to 50 percent of the country's annual GDP -- fiscal stability certainly preferable to the precarious, hand-to-mouth, condition of our Social Security system.

However, while I strongly favor a free trade relationship with Chile, I do not favor it at any political price. This administration's demand that future trade negotiations address worker righ's and environmental protection with sanctionable enforcement mechanisms is misguided and wrong. In trying to reach agreement on the scope of future fast track authority, Republicans have tried in good faith to accomodate the Administration's concerns about these issues. Unfortunately, we have found them unwilling to seek any middle ground. Nonetheless, I remain hopeful that, at some point, we can reach agreement on these important issues and move forward toward hemispheric free trade with a bi-partisan consensus.

Conclusion

A decade ago, the Mexican peso crisis would have been enough to send all of Latin America into a tailspin. But nations throughout the hemisphere, most notably Chile, did not let the shock waves of Mexico halt their own progress toward economic liberalization.

Economic liberalization and political freedom go hand-in-hand. This has been demonstrated many times in this hemisphere and throughout the world. Our trade policies must reflect this truth. It is critical that we promote a world economy open to the broadest range of economic transactions. We must not be seduced by the short-term political benefits of protectionism and economic nationalism. Economic growth is not a zero-sum game. If others get richer, the U.S. does not get poorer.

Increased trade is imperative if we are going to improve the American standard of living and create high-wage jobs. Though we have never had a self-contained economy, there was a time when we were nearly self-reliant. But that era passed a long time ago. Now our economy is increasingly reliant on the economies of other nations as a source of growth, job creation, and rising national income.

In fact, in the last five years, U.S. export growth has accounted for 50 percent of total U.S. economic growth. The U.S. Trade Representative has estimated that trade will continue to grow in importance and account for 36 percent of GDP by 2010 -- up from just 14 percent just 25 years ago. That means that, in 15 years, more than one-third of our standard of living will depend entirely on our ability to do business with other nations. We can not ignore the reality that trade is of critical and increasing importance to our economic future.

America has nothing to fear from open trade. Tariffs do not protect domestic producers; they

protect ill-considered government policies-- costly regulations, high taxes on labor and capital-- policies that only serve to reduce the standard of living for our own citizens and stifle economic opportunities for other nations. That is what cripples American manufacturers -- not foreign competition. If you doubt this, look at Japan. There you find an enormously powerful economic engine, but a standard of living far below that of other industrialized countries.

The idea that government-directed tariffs and quotas can protect domestic markets contradicts the fundamental principle of the free market. History demonstrates, over and over again, that governments will usually do the wrong thing when it comes to directing markets. That is why we need less government interference in both domestic and international economic affairs.

This is why I believe we should move forward in advancing the goal of hemispheric free trade. It is a win-win proposition for the United States -- it will advance the interests of democracy throughout the hemisphere and it will help to ensure long-term economic prosperity for the United States.

Thank you again for the opportunity to testify today.

Congress of the United States
House of Representatives
Washington, DC 20515

Testimony of Congressman Duncan Hunter
Before the House International Relations Subcommittee
on International Economic Policy and Trade

October 24, 1995

Mr. Chairman, I appreciate the opportunity to be here today to testify on an issue that is sure to have a direct impact on the well-being of our nation's economy. Specifically, I am here today to highlight the potentially dangerous results of allowing the nation of Chile to join the North American Free Trade Agreement (NAFTA).

As you may be aware, since its start, NAFTA has failed to show even a fraction of the economic gains promised by many of the agreement's supporters. Issues like industrial relocation, a weakened Mexican Peso and continuous implementation disputes clearly illustrate the need to re-think any attempt to expand this pact.

Chile currently maintains a relatively open economy with few protective trade barriers. The idea that somehow the U.S. economy will benefit from increased access to Chile's consumer market is questionable. In fact, at a briefing conducted on June 23 by the U.S. Trade Representative's office and the Commerce Department, U.S. exports, related to the possible expansion of NAFTA, were not even discussed.

Mr. Chairman, I believe that a much larger issue is at stake. The motivating factors behind efforts to include Chile in NAFTA is to establish a precedent for future expansion. By bringing Chile into NAFTA, the natural next step would be to introduce various other Latin American countries into the pact. The real issue is not the opening of Chile, but the opening of NAFTA.

The original purpose of NAFTA was to facilitate trade surpluses with member nations as a method of negating our trade deficits with Asia and Europe. Since the passage of NAFTA, Mexican exports to the U.S. are up 29 percent. During the first six months of this year, imports from the U.S. are down 12 percent. The U.S. trade surplus with Mexico has not only evaporated, but has also degenerated into what is expected to result in a $20 billion deficit by the end of the year. To suggest that expanding NAFTA to the far reaches of the Western Hemisphere will result in more jobs for the U.S. is not supported by the facts.

In 1993, NAFTA proponents promised that the presence of U.S. industry and the expected increase in trade with Mexico would provide the citizens of that country with the financial ability to purchase U.S.-manufactured products. Based on an artificially high peso, the Mexican economy seemed poised to expand and to explore increased trade activity.

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Unfortunately, in the year following the enactment of NAFTA, the actual state of Mexico's economy became painfully apparent to the world community, especially to the United States.

In 1994, the Mexican economy suffered one of its worst years in recent memory. As the result of political corruption, internal strife and investor skepticism, Mexico's international reserves plunged downward in late November from $17 billion to under $6 billion in less than two days. On December 22, 1994, the Mexican Government adopted a floating exchange rate for the Peso, without protecting its financial markets. The result was an economic collapse.

Since Mexico did not have the necessary international reserves to meet payments on its Tesobonos (Dollar–linked government bonds) of $10 billion, the newly formed Zedillo government was forced to turn to its NAFTA partner, the United States. On January 12, 1995, the Zedillo Administration began efforts to lobby President Clinton to provide an unprecedented $53 billion in direct financial assistance.

By January 31, 1995, President Clinton had agreed to funnel this assistance from primarily three sources: $20 billion from the U.S. Treasury's Economic Stabilization Fund (ESF), $17.8 billion from the International Monetary Fund (IMF) and $10 billion from the Bank for International Settlements (BIS). From this pool, Mexico has already borrowed over $25 billion, with $12.5 billion coming directly from the Treasury's ESF. It is important to understand that these funds are not being used to rebuild Mexico's economy, but merely to restructure the country's debt. The money is going to Mexico's past, not its future.

In providing the recent $700 million installment payment to the U.S., Mexico attempted to show its ability to pay its debts. Unfortunately, the remaining $1.3 billion of this short–term installment will not be repaid on time. Thus, the "early" payment on the eve of President Zedillo's visit to Washington was just another public relations ploy reminiscent of those which misled American opinion during the debate on NAFTA and Mexico's viability.

With increased inflation, excessive interest rates and a shrinking economy, Mexico is clearly not becoming the economic partner NAFTA supporters originally envisioned. The effect of these economic variables has resulted in a reduction in consumer purchasing power of close to 30%. Mexico's consumers cannot purchase enough American exports to strengthen its economy. President Clinton claimed U.S. exports to Mexico are still healthy, but these are mainly components being sent to Mexican factories to be converted into goods and re–exported back to the U.S.

On the other hand, the prediction by its opponents that NAFTA would have the negative effect of industrial flight is manifesting itself. So far in 1995, 47 of our nation's companies have committed nearly $500 million to new maquiladora plants in Baja alone, producing goods that can only be sent into the U.S.

Additionally, according to recently released Commerce Department figures, the U.S. deficit in manufacturing trade has reached $118.1 billion in the first eight months of this

year. Although these type of figures are all too familiar, it should be noted that the small merchandise trade surplus with Mexico, enjoyed by the U.S in 1994, has evolved into a $10.0 billion deficit already this year. Mexico has become part of the problem, not part of the solution.

During the NAFTA debate, many of the agreement's proponents claimed that by entering into this contract, the U.S. would not become responsible for the economies of their prospective partners. In fact, many of NAFTA's opponents were often derided for suggesting that as a means of ensuring the pact's livelihood, the U.S. would eventually be forced to guarantee the financial well-being—and perhaps the political stability—of the other NAFTA members. Not only has the U.S. given billions of dollars in assistance to Mexico, but also as a result of the bailout agreement, our nation has imposed rigorous monetary, fiscal and structural policy targets on its economy. These targets include the pursuit of a tight monetary policy with negative real growth coupled with reduced government spending and further privatization of industry and banking. Mr. Chairman, I highly doubt that even the most ardent NAFTA supporter ever intended the U.S. to assume responsibility for managing the fundamental restructuring of Mexico's economy.

Finally, I would again question the motives of those who would seek to bring Chile into NAFTA. As I have stated, the present agreement has only resulted in domestic industrial flight, while also forcing the U.S. to adopt control of a sovereign nation's economy. The idea of someday expanding NAFTA to include many or all of the Western Hemisphere's countries must certainly be re-examined. We cannot afford to protect, secure or guarantee the productive power of our often unstable Latin American neighbors.

Mr. Chairman, I would again like to express my sincere gratitude for the chance to address your subcommittee on this pivotal issue. It is my hope that as Congress further considers the prospect of expanding NAFTA, open and conclusive hearings such as this are maintained.

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UNITED STATES
HOUSE OF REPRESENTATIVES

COMMITTEE ON WAYS AND MEANS

SUBCOMMITTEES
TRADE
HUMAN RESOURCES

HOUSE OVERSIGHT
COMMITTEE

STATEMENT OF HON. JENNIFER DUNN
OCTOBER 25, 1995

HOUSE INTERNATIONAL RELATIONS COMMITTEE
JOINT HEARING of the
WESTERN HEMISPHERE and
INTERNATIONAL ECONOMIC POLICY and TRADE SUBCOMMITTEES

• • •

Thank you, Chairman Burton and Chairman Roth, for this opportunity to testify.

As a member of the House Ways and Means Trade Subcommittee, and as one who has travelled to Chile twice since May, I have seen with my own eyes why we should move forward as soon as possible with expanding membership in NAFTA to the nation of Chile. It is good for the United States and it is good for Chile.

Before my first trip to Chile, I assembled a broad cross-section of Washington State businesses involved in trade with Chile. Represented was everyone from the forestry industry to trucking, apples to computer software. I was surprised to learn the degree to which my state is trading with Chile. Since 1987, Washington State's trade with Chile has increased 170 percent: food products are up 852 percent, transportation equipment up 679 percent, scientific instruments up 812 percent.

My message, in a nutshell, Chairmen, is that Chile is stable and economically advanced, and it is to the mutual benefit of both countries to increase our trade. I have heard Chile compared more often to Singapore and other rapidly-growing countries in the Asian Pacific Rim than I have to neighboring Latin American nations. A measure of Chile's stability is implicit in the remark of a representative from one of those Washington State-based companies, who told me, with all due respect to Congressman Hunter, that "investing in Chile is less risky today than investing in California."

The growth of the Chilean economy over the last 20 years has been dramatic, a success story by anyone's standards. Simply look at the facts:

- For nearly a decade, the Chilean economy has grown at a steady, average rate of 6.8%. We should be so fortunate.

- With growth comes demand -- and in Chile, the demand is for U.S. products. Last year, Chilean demand for U.S. goods amounted to a contribution equivalent to $2.3 billion to our economy. Meanwhile, U.S. exports to Chile accounted for 23 percent of that country's imports.

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Hon. Jennifer Dunn
October 25, 1995

Increased demand for U.S. products means U.S. firms will sell more goods: more Washington State apples, more vehicles, more computer equipment. *This means jobs*, ladies and gentlemen. Not only in my home state, but nationwide. And more jobs result in increased economic growth for the United States and greater prosperity for Americans.

- The Chilean market is one of the most barrier-free in Latin America -- tariffs have dropped to an across-the-board 11 percent.

- The United States is the largest investor in Chile today because Chile presents an extremely safe, low-risk and profitable investment. In fact, U.S. exports to Chile have grown by well over 200 percent since 1987.

- Because of widespread privatization and a dramatic savings rate (the savings rate in Chile is an astounding 26 percent of gross domestic product!), Chile is not reliant on foreign investment or capital.

Which is why, unlike many countries in the region, Chile was able to insulate and protect itself from any adverse effects resulting from the devaluation of the Mexican peso. This is the mark of sound monetary policy and a healthy economic structure.

As important as I view the growth of Chile's strong economy, I am also challenged to look at the performance of NAFTA since its commencement in January 1994. While I recognize that some of my colleagues hold different perspectives on NAFTA, U.S. exports to NAFTA members are growing twice as fast as to the rest of the world. As my good friend Mr. Kolbe has pointed out, U.S. exports to Mexico exceed $1 billion *each week*.

In 1994, my home state of Washington outranked 33 states in terms of exports to Mexico, with sales in excess of $477 million. Washington State's exports to Mexico during last year increased 58.5 percent from the previous year (1993). In fact, since NAFTA's implementation, Mexico has become the top export market for Washington State apples. So, NAFTA is creating jobs -- good jobs -- in Washington State.

In gauging the potential benefits to the United States of expanding NAFTA, we should consider not only the economic advantage of freer trade with Chile, but the increased ability to influence the trade policies of neighboring countries in the region and the progress made toward a Free Trade Agreement of the Americas (FTAA). The FTAA, after all, is the ultimate goal.

Hon. Jennifer Dunn
October 25, 1995

To quote The Wall Street Journal (February 3, 1995) "...there exists a very real threat that Chile's planned membership... will fall victim to the revival of NAFTA detractors..." Who would have guessed, incidentally, that added to that threat would be the Clinton Administration, the very folks who extended the invitation for Chile to join NAFTA in the first place?

That's right. Let me add that were it not for the Administration's unwillingness to work with the Congress on fast-track authority, the United States Congress would, in all likelihood, be poised this week to offer the positive results of its vote on fast track authority as a signal of its support of Chilean accession to NAFTA.

On the one hand, to attempt to include so many non-trade related matters in a trade negotiation bill is, in my view, highly, *highly* inappropriate. However, in an attempt to work with the Clinton Administration in the customary bipartisan fashion accorded to trade issues, every request was accommodated, and every concern was answered. In light of the fact that it is not the duty nor the function of the Executive Branch to dictate legislative policy to the Congress, there comes a point when the Congress must assert itself. Once reminded of its role in drafting legislation granting fast-track authority, it was the Administration that walked away from tne table. Make no mistake: refusing to work with Congress on this matter will have untold consequences for small businesses and industries that do business with Chile. In my view, the Administration would be well-advised to put domestic politics aside and promote our economy.

What happens if this opportunity is allowed to slip by? Clearly, the benefits to the United States of a completely open Chilean market will be lost. Who knows for how long? And what will be the effect in terms of lost confidence? Yet there's perhaps a more important factor. Can you put a price on the value of having Latin American countries adopt and promote American business standards -- such things as the treatment of investments or intellectual property rights? What is the value of lost opportunities, lost jobs, and lost revenue each month we haven't met our goal of having a Free Trade Area of the Americas? In this hemisphere, the nations to our south are looking toward Chile as a role model -- a nation to learn from. After visits to Latin America and meetings with the region's political leaders, there is no question that it is in the U.S. interests to build upon our trade relations in Latin America.

In view of the successes of NAFTA, the fact that U.S. exports are up 22 percent to our NAFTA trading partners, expanding the agreement to include one of the hemisphere's most competitive, most trade-sophisticated, most promising countries is the next natural step. I thank the Committee for the opportunity to present my views and will be happy to answer any questions.

* * *

STATEMENT OF THE HONORABLE DONALD MANZULLO
BEFORE THE SUBCOMMITTEES ON INTERNATIONAL
ECONOMIC POLICY AND TRADE AND ON
THE WESTERN HEMISPHERE OF THE
HOUSE INTERNATIONAL RELATIONS COMMITTEE
October 25, 1995 10:00 AM in Room 2172 RHOB

Thank you, Mr. Chairman, for holding this hearing today on the accession of Chile to the North American Free Trade Agreement (NAFTA).

I expect today we will hear from the doomsayers that NAFTA has failed because of the devaluation of the Mexican peso. However, they ignore two key critical points.

First, NAFTA has retained preferential access for U.S. and Canadian products in the Mexican market. Despite the peso crisis and the need to curtail imports, Mexico has continued to proceed with the tariff reduction schedule as required under NAFTA. However, at the same time, Mexico has raised tariffs against all other trading partners outside of NAFTA to restrict capital outflows from Mexico.

That's why U.S. merchandise exports to Mexico have increased 9.8 percent since NAFTA's implementation in 1993 while exports from other nations to Mexico have suffered serious decline. These U.S. exports to Mexico support 2.5 million U.S. jobs, which is an increase of 340,000 since 1993.

Contrast this with the Mexico action to U.S. exports during a previous economic crisis in 1982. During that difficult time, Mexico raised tariffs on all goods entering their country. As a result, U.S. exports to Mexico were cut by about half. Thus, in 1995, NAFTA has retained preferential access for U.S. exports to Mexico, unlike 1982.

Second, NAFTA has locked into Mexican law basic standard U.S. business practices. There has been no effort in Mexico to repeal economic reforms precipitated by NAFTA such as customs processing and intellectual property rights protections. In the long run, NAFTA will benefit overall U.S. economic interests.

Then, why not begin the process of extending these benefits to other nations in Latin America? I can think of no better candidate than Chile. Growth rates in Chile have averaged over six percent each year over the past 10 years, similar to the economic dynamism one can find in Taiwan, South Korea, Singapore, and Hong Kong. As a good role model for the United States, Chile continues to run a budget surplus each year, mainly due to its relatively large savings rate. Chile's free market economic policies have pulled a half million of its citizens out of poverty, which is equivalent to 20 to 25 million people in the United States.

The average tariff rate for Chilean goods entering the U.S. market is less than one percent. On the reverse side, the average tariff rate for all goods entering Chile is 11 percent. Thus, Chile has already a basically one-sided free trade relationship with the United States.

Chile is also in the process of negotiating a variety of free trade arrangements with its Latin American neighbors, the European Union, and Japan. If the United States Congress stops trade negotiations with Chile by not enacting "fast track" legislation, it will make it much harder for U.S. exports to penetrate the Chilean market. Our other economic competitors could have a zero tariff rate while U.S. products would be subject to an 11 percent entry fee tax, making our goods less affordable in Chile throughout the years to come.

Chile wants American products. U.S. exports to Chile have already increased four-fold since 1985. In Illinois alone, exports have grown 191 percent, going from $75 million in 1987 to $219 million in 1994. Some of the largest growth increases have been in products made in the 16th Congressional District such as industrial machinery and computers (280 percent) and transportation equipment (228 percent).

Halting Chilean accession to NAFTA will not reverse the economic problems still facing Mexico. I encourage my colleagues to look at Chile separately on its own merit. In many respects, Chile is the most developed country in Latin America. It makes no sense to penalize Chile and our exporters by denying "fast track" legislative authority to the U.S. Trade Representative. Let's empower American exporters by allowing them to sell goods and services made by U.S. workers to Chile on a zero tariff basis.

Finally, Mr. Chairman, I ask unanimous consent to insert into the hearing record a copy of an article written by our colleague, Representative David Dreier of California, and a recent editorial from the Rockford Register Star on NAFTA.

Thank you, Mr. Chairman. I look forward to the testimony of the witnesses here before us today.

TESTIMONY OF IRA S. SHAPIRO BEFORE THE SUBCOMMITTEE ON THE WESTERN HEMISPHERE AND THE SUBCOMMITTEE ON INTERNATIONAL ECONOMIC POLICY AND TRADE OF THE HOUSE COMMITTEE ON INTERNATIONAL RELATIONS OCTOBER 25, 1995

Introduction

Mr. Chairman, I welcome the opportunity to appear today before the Subcommittee on the Western Hemisphere and the Subcommittee on International Economic Policy and Trade to discuss our experience during the first 21 months of the North American Free Trade Agreement (NAFTA) and the important role it plays in a larger U.S. strategy to build the Free Trade Area of the Americas (FTAA).

Let me begin by emphasizing the importance of expanding trade to the United States.

First, expanding trade is critical to our efforts to create good, high-wage jobs. In 1970, the value of trade equaled just 13 percent of the U.S. GDP. If current trends hold, that figure will exceed 30 percent in 1995, with more than $2 trillion dollars in trade relative to a $7 trillion economy. Over 12 million workers in this country owe their jobs to exports. On average, these jobs pay 13 -17 percent more than non-trade jobs. Every billion dollars of exports supports an estimated 15,000 jobs.

Second, with a mature economy, only 4 percent of the world's population, and near-zero population growth, future opportunities for U.S. economic growth and the jobs it creates will come from the other 96 percent of the world's population. For example, Latin America and the Caribbean now has the second fastest economic growth of any region in the world, with 400 million inhabitants. Our ability to create jobs and foster economic growth in this country depends on expanding trade with dynamic economic regions around the globe. To paraphrase Willie Sutton, that's where the customers are.

Third, the United States is a very open market, with very low average tariffs and largely open investment and services regimes. Since most other countries have significantly higher barriers to our goods and services, reciprocal trade agreements mean the United States benefits from relatively larger concessions on the part of our trading partners. For example, tariffs in Latin America and the Caribbean average four times the U.S. average tariff rate, even after the dramatic reduction in tariffs in the region in recent years that has helped stimulate growth and trade.

Fourth, as the world's largest single market, the United States is a tremendously attractive place to

do business for countries around the world. The size of our markets makes us an attractive partner to negotiate trade agreements with. In fact, all the 34 democratically elected Leaders of Latin America and the Caribbean - including all the countries in the Americas but one - have committed their countries to pursue the FTAA. It is fair to say that a free trade area with the United States is the main attraction in the FTAA process for virtually all the countries in this hemisphere -- an attraction for which they are willing to open markets, remove barriers, and improve economic regulation in a variety of areas of interest to us.

A final reason is leadership. In this 50th anniversary year of the end of the Second World War, we have celebrated the success of the U.S.-led coalition that ended that bloody conflict and created an international system that has avoided a global war for half a century, and nearly eliminated the hold of totalitarianism on citizens around the globe. Over the same period, the United States has also led the world away from high tariff walls that kept markets isolated from one another, and from higher levels of growth. Now, after the Cold War, global economic competition has risen to replace global competition over political ideologies. Increasingly, our ability to lead the world depends on a strong economy, and the strength of our economy increasingly depends on us leading the world to more open markets and expanded trade.

Mr. Chairman, President Clinton understands these imperatives affecting our nation and he built a trade policy which reflects them. It is an approach that builds on the one chosen by Presidents of both parties, with bi-partisan support in Congress for the last fifty years, by supporting the movement toward open markets, but it sets a new course as well by insisting on reciprocity. In other words, we seek open markets, but we insist that other nations accept responsibility in maintaining open markets. Our trade agreements must be "single undertakings" where everyone plays by the same rules. The global economy will only succeed if the playing field is level. More importantly, American workers expect fairness and we insist on it.

Since the Clinton Administration began, the United States has led the world on the greatest movement toward free and fair trade in history. We have concluded over 150 trade agreements, including the North American Free Trade Agreement, the Uruguay Round and historic trade agreements with Europe, Japan and China. Many of these successes occurred because of our willingness to enforce our trade laws if other nations were not living up to their agreements, or were acting uncompetitively. We have set the stage for trade expansion in Asia through the Asia Pacific Economic Cooperation forum with the Bogor Declaration; and announced creation of a Free Trade Area of the Americas by 2005 at the historic Summit of the Americas. And we have led the world in addressing issues which affect trade but were previously considered out of bounds in trade agreements, including corruption, labor and the environment. By leading, we have ensured -- and will continue to ensure -- that these agreements were shaped on our terms.

Many of these efforts will not reap benefits for years. But President Clinton has laid the groundwork for decades of growth. Already the jury is in on much of President Clinton has accomplished. The President's work on trade has contributed to an unprecedented export boom and created hundreds of thousands of high-paying jobs.

The growth in merchandise exports since President Clinton entered office has been stunning. In 1993, exports grew 4 percent, in 1994, 10.2 percent. This year, exports are up by more than 16 percent.

That means growth in good, high wage jobs. In the first three years of this Administration, 1.6 million jobs will have been created by exports. On average, these jobs pay 13 - 17 percent more than non-trade jobs.

President Clinton believes the United States must lead to shape this changing world so it benefits all Americans. He knows U.S. workers and companies are the most competitive and productive in the world and they can meet any challenge. By embarking on this course, President Clinton is keeping our nation strong by asserting leadership abroad.

One of our most important efforts to create jobs and assert U.S. leadership in the global economy has involved expanding trade with this hemisphere. Today, I would like to address our initial experience under the Agreement and explain the importance of the NAFTA to our ability to continue expanding U.S. jobs, trade and competitive opportunities throughout the Americas, starting with Chile.

NAFTA Has Built a Foundation and Been A Success

During the debate over the NAFTA two years ago, this Administration argued that the NAFTA would provide several benefits to the United States. We entered into the NAFTA because of the need to expand trade in order to create jobs and economic growth, and to raise our standard of living and remain competitive in an increasingly competitive world.

A free trade area with Mexico offered the United States several advantages:

- Mexico is our third largest export market, with a tremendous preference for U.S. goods: over 70 cents of every dollar spent on imports in Mexico goes to goods from the United States;

- Mexico had substantially higher barriers to trade and investment than the United States -- meaning that an agreement to eliminate barriers created relatively greater opportunities for U.S. firms; and

- Mexico shared our interest in a trade agreement that would go beyond trade in goods to address other key areas of our concern and set high standards for the world to emulate.

What does the first 21 months of experience under the NAFTA show, and how does it match up with our expectations on jobs, exports, wages and competitiveness?

- U.S. exports to both our NAFTA partners have increased by 22 percent since 1993, despite Mexico's financial crisis.

- In NAFTA's first year alone, trade among the NAFTA partners grew by 17 percent. In that year, U.S. merchandise exports to Mexico and Canada grew by 16 percent -- over twice as fast as U.S. exports to the rest of the world. U.S. exports of semiconductors, machine tools, rice and even adhesives surged as Mexican trade barriers came down - and continued to increase in 1995.

- Merchandise exports to Canada and Mexico currently support an estimated 2.5 million U.S. jobs. These export-related jobs pay 13 to 17 percent more than the average wage.

In addition, it is important to emphasize the success of our trade relationship with Canada, which in the heated debate over NAFTA we often forget is the other partner in NAFTA. Our desire in creating the NAFTA was to build on the U.S. - Canada Free Trade Agreement (CFTA), which took effect on January 1, 1989, created the world's largest and most comprehensive bilateral free trade area.

It is also important to emphasize that the NAFTA improved on -- and superseded -- the CFTA not only in adding the large and growing Mexican market to the free trade area, but also in providing stronger substantive provisions that expand on our previous relationship with Canada.

The NAFTA has clearly benefited the United States with respect to our trade with Canada. For example:

- Total merchandise trade with Canada exceeded $243 billion dollars in 1994. When you include services, bilateral trade with Canada approaches $300 billion. U.S. exports to Canada in the first eight months of 1995 were $84 billion, a 15 percent increase over the same period in 1994. U.S. imports from Canada during the same period were $95 billion, a 17 percent increase over last year.

- Goods exports to Canada rose approximately 50 percent from 1988 to 1994, from $71.6 billion to $114.2 billion. This increase in trade is all the more remarkable in light of the low rate of growth in overall GNP, especially in Canada, in the early 1990's.

- Since implementation of the CFTA in 1989, U.S. trade with Canada has grown 17 percent faster than U.S. trade with the rest of the world. Most of this growth has taken place over the last two years, when bilateral trade has soared. By 1994, the majority of duties on bilateral trade had been eliminated; even those products deemed most sensitive have had their duties cut in half.

- U.S. export growth in recent years has been heavily reliant on Canadian sales, with Canada accounting for 37 percent of the increase in U.S. exports since 1992.

Impact of the Peso Crisis

The NAFTA partners expected to implement the agreement during a period of relative calm and economic growth. Political assassination, natural disasters and a balance of payments crisis have made Mexico's experience over the last two years different from what was desired both here and in Mexico. Some have cited these unfortunate developments to claim that the NAFTA was a mistake. However, consider the following:

- U.S. exports to Mexico have grown since NAFTA took effect, despite this year's temporary slow-down in Mexican economic growth. In the first eight months of 1995, U.S. merchandise exports to Mexico totaled $30.1 billion, up by 9.8 percent from the same pre-NAFTA period in 1993. 700,000 U.S. jobs are supported by trade with Mexico.

- Because of NAFTA, U.S. exports have fared much better this year than after the Mexican financial crisis in 1982. In 1982, the Mexicans imposed 100 percent duties on American products, a move that cut our exports to Mexico in half. It took 6 years to recover. If the same thing had happened this year, U.S. exporters would have lost $25 billion in sales and not recovered until the year 2000.

- Instead of retreating into protectionism, Mexico actually cut its tariffs on U.S. products in January 1995 in accordance with NAFTA provisions, and maintained existing NAFTA tariff cuts.

  - In contrast, Mexico raised tariffs on some goods from non-NAFTA partners by 15 percentage points. Partly as a result, the U.S. share of Mexico's import market grew from 70 percent in 1994 to 73 percent in the first half of 1995.

- Mexico is also going beyond its NAFTA obligations by liberalizing financial services and embarking on a round of further privatization in the transportation, telecommunications, and petrochemicals markets. This will create new opportunities for U.S. businesses and workers.

Mexico's economic crisis has affected U.S. exports to that country, as would be expected regarding any country that experiences a devaluation and severe economic contraction. Trade agreements cannot guarantee that any country will set a permanent smooth course to prosperity. Our trade agreement partners still must bear responsibility for their basic economic management.

NAFTA did not cause Mexico's short term balance of payments problem. But we can be sure that without NAFTA the Mexican government easily could have chosen the self-defeating path it chose in past similar crises: raising walls of protection, and limiting U.S. exports. An important test of an agreement is how it works in unfortunate times. NAFTA has passed this test, and passed it well.

The NAFTA Mechanism for Cooperatively Addressing Worker Rights and the Environment

NAFTA was the first comprehensive trade agreement accompanied by agreements on labor and environmental issues related to trade. These provisions ensure that expanded trade supports the improvement of labor and environmental conditions and the enforcement of national labor and environmental laws.

As a result of the NAFTA labor agreement, the Ministers of Labor of the three NAFTA countries have held two council meetings in which they discussed a broad range of issues, including union registration, health and safety, and wage and compensation issues. In addition, 5 submissions related to the enforcement of labor law in Mexico and the United States have been reviewed. This review process provides an important mechanism for Mexican and American workers to raise concerns about labor law enforcement.

In the past two years, the United States and Mexico have made progress in protecting our environment and our public health -- thanks to efforts set in motion by NAFTA's environmental agreement. The institutions established by NAFTA are working with affected state and local governments and the public to develop solutions to environmental problems such as unsafe drinking water and inadequate municipal waste disposal and sewage treatment affecting border communities in Texas, New Mexico, California, and Arizona.

NAFTA makes both economic and environmental sense. For example, Mexico's much-strengthened pollution controls have resulted in an increased need for U.S. technology and expertise.

Chile and Latin America: The Case for Moving Forward

Just as the United States has a strong interest in a healthy and growing trade relationship with Mexico, the United States has a strong economic interest in moving forward now with an ambitious and timely trade agreement agenda in the Western Hemisphere. Chile's accession to NAFTA is an essential component of a two-part strategy to shape and pursue this hemispheric agenda.

The first element of the strategy is to build stronger trade relations with all the countries in the hemisphere with which we are not yet prepared to enter into full-fledged free trade agreements. The process of building a Free Trade Area of the Americas is a huge undertaking, and we must do what we can now to lay the groundwork and advance the process in every corner of the hemisphere. In this connection, following the Summit of the Americas in December 1994, Ambassador Kantor hosted a meeting of trade ministers in Denver on June 30, 1995, which created hemispheric working groups addressing a variety of trade issues: market access for goods, technical barriers to trade, investment, sanitary and phytosanitary measures, anti-dumping and countervailing duties, customs procedures, rules of origin, and the smaller economies. Additional working groups covering intellectual property rights, government procurement, cross border

services and competition policy will be established at the follow-up hemisphere trade ministerial meeting in March 1996. Through these working groups the United States intends to exercise leadership toward lowering barriers and establishing disciplines that will facilitate trade, investment, and economic growth in the hemisphere, and pave the way for the FTAA.

But ultimately, the ability of the United States to lead the hemisphere toward an FTAA with strong disciplines and broad market-opening depends on our ability to set high standards through the NAFTA accession process. Access to the large U.S. market -- or the integrated North American market -- remains the "prize" for the rest of the hemisphere and the motivation for agreeing to the strong disciplines and broad market-opening measures that we seek in return. Expanding the NAFTA to other countries now further increases the size of the market that could be available to other countries in the future if they meet NAFTA's high standards.

Simply put, NAFTA accession will build momentum for the U.S.-led trade agenda for the hemisphere. There is plenty of competition in the region from other countries with other agendas. The hemisphere contains numerous sub-regional free trade arrangements reflecting a diversity of objectives and traditions that are largely uninfluenced by the United States In recent years, countries in the region have accelerated their efforts to reach free trade agreements, and some of the agreements have become more comprehensive, although not as comprehensive as the NAFTA. It is critical that the United States contribute tangibly to the ongoing sub-regional process in Latin America and the Caribbean to balance and help shape the free trade agreement agenda in the Americas by moving forward with Chile. In this way, the United States will ensure that U.S. exporters, service providers and workers get a fair shake at the second fastest growing markets in the world.

In addition, building a comprehensive trade relationship with Chile has broad strategic trade policy attractions. Chile is negotiating a free trade agreement with MERCOSUR. Chile is also a member of the APEC. Chile therefore is a trade policy gateway to MERCOSUR and South America, and Chile's accession to the NAFTA will bring to four the number of APEC members participating in North American free trade.

For many years the United States had a very limited trade relationship with Latin America, one that held little promise for the future due to Latin America's inward-looking economic and trade policies. Now that has dramatically changed. A market-based economic policy transformation, coupled with a renewed commitment to democracy, has turned a region with little promise into a region that inspires. Officials from the World Bank, for example, recently issued a report indicating that growth in Latin America could accelerate to more than six percent per year over the next few years, thus providing even more new opportunities for our exporters. Latin America is already the second fastest growing region in the world. U.S. exports to Latin America already approximate our exports to Western Europe, and if current trends continue they will exceed those to Western Europe and Japan combined by the year 2010. This upward trend and the opportunities that it has brought -- 762,000 new higher-than-average paying U.S. jobs during the 1985-95 period -- will only be sustained with sound macroeconomic policymaking in Latin

America and the United States and an aggressive and ongoing effort to open markets to the benefits of trade on a more level playing field. Over 1.36 million U.S. jobs are related to exports to Latin America and the Caribbean as of 1995. Many of our competitors, including the EU, have also noticed the prospects for major trade and the resulting job gains and are acting to ensure their interests are protected with their own trade agreement strategies with the region.

Two successive Presidents have been committed to the pursuit of a free trade area with Chile. No other country in Latin America has a better record of economic accomplishment in the last ten years than Chile. Chile is a pioneer. If the United States seeks broadly to encourage stable, growth-sustaining policies and the adherence to open markets, there is no better country in the region with which to set an example. Chile weathered a very difficult economic period in the early 1980s characterized by dramatically reduced economic output and an unemployment rate of 20 percent. It learned valuable lessons regarding the management of its economy which serve it well today. Chile's economic accomplishments are outstanding. Let's examine some facts:

- Chile was recently voted by the highly regarded Davos Economic Forum the fifth most competitive emerging economy in the world;

- Chile's average economic growth rate since 1985 has been over 6 percent, putting it on par with the most dynamic economies of the Asian Pacific Rim;

- Chile's growth rate is expected to reach 7 percent this year, with inflation at under 8 percent on an annualized basis continuing its downward trend and unemployment continuing to trend downwards at 5.6 percent;

- Chile's currency has been appreciating against the dollar, and Chile is taking the unusual of step of paying its obligations in advance of when they are due to the international financial institutions, such as the Inter-American Development Bank;

- Chile's market-based economic policies have lifted over one million people above the official poverty line since the transition to democracy in 1990 -- out of a total population of 13 million. The same ratio in the United States would have meant lifting approximately 20 million people above the poverty line since 1990;

- Chile led Latin America's movement toward comprehensive privatization;

- Chile's national savings rate was a strong 24 percent of gross domestic product during the 1990-93 period;

- Chile's national investment rate was an astounding 27 percent of gross domestic product during the 1990-93 period, the highest in the region;

- Chile has run a surplus in its national budget for eight straight years, and is expected to

do so again this year, with public savings accounting for almost five percent of gross domestic product in 1994;

- Chile's foreign reserves are high and rising;

- Chile's financial system is strong -- the Chilean banking sector averaged 19 percent profitability on an annual basis over the last 10 years, and Standard and Poor's recognized its banking supervisory bureau as the best in Latin America;

- Chile's trade regime is characterized by a uniform tariff rate of 11 percent ad valorem across the board with virtually no quantitative restrictions;

- Chile was the first developing country to bind its tariffs across the board in the Tokyo Round of multilateral trade negotiations in 1979;

- Chile was an active contributor to the Uruguay Round of multilateral trade negotiations;

- Chile is a new and valued member of APEC; and

- Chile has one of the most aggressive free trade agreement agendas in Latin America, having concluded agreements (which address primarily tariffs and quantitative restrictions) with Mexico, Colombia, Venezuela and Ecuador and less comprehensive agreements with Argentina and Bolivia. In addition, and as indicated earlier, Chile is negotiating a free trade agreement with the MERCOSUR and has also agreed with the EU to pursue a trade agreement.

United States - Chile Trade: A Model for Growth

U.S. - Chile trade has increased dramatically. The vibrancy of the trade relationship is an example we would hope to repeat across the region. U.S. exports to Chile quadrupled during 1985-94, growing from $682 million to $2.8 billion. U.S. exports have again jumped by 33 percent when comparing the January - July period in 1994 to 1995. Virtually every state in the United States dramatically increased its exports to Chile from 1987 to 1994, with 42 states more than doubling their exports to Chile during the same period. States with the biggest dollar gains in exports to Chile during the 1987-94 period include Florida, California, Illinois, Texas, New Jersey, New York, Michigan, Connecticut, Georgia and Wisconsin, with industrial machinery, computers, transportation equipment and chemicals the largest single sectors in 1994 U.S. exports. Last year, the United States ran a trade surplus with Chile of nearly $1 billion. During the 1987-94 period, U.S. exports of:

- transportation equipment increased 757 percent;

- chemical products increased 85 percent;

- industrial machinery and computer products increased 254 percent;
- electronic equipment increased 356 percent; and
- textile mill products increased 212 percent.

The Accession Negotiations

The negotiation of Chile's accession to the NAFTA will remove significant remaining barriers that impede U.S. exports to Chile and thus further increase the potential for export gains. The NAFTA and its related agreements cover a broad spectrum of disciplines. Chile's adherence to these rules will help to upgrade trade and regulatory practices and policies in Chile that will ensure a continually growing and mutually productive trade relationship. Chile's adherence to the NAFTA disciplines will also encourage in the most concrete way movement by other important trading partners in the region towards disciplines that benefit U.S. traders, workers, investors and service providers.

Consistent with past practice for free trade agreements, the Administration solicited and received the advice of the U.S. International Trade Commission on the economic implications for the United States of Chile's accession to the NAFTA. We have also solicited and received advice from our official advisory committees, including from the membership of the Advisory Committee on Trade Policy and Negotiations (ACTPN) and the sectoral and functional committees. Our negotiators will continue to seek the views of the advisory committees as we proceed. The Administration has also sought and received advice from the public and welcomes any additional advice interested parties wish to provide. Most importantly, the Administration is committed to continuing our consultations with Congress as we proceed in our effort with Chile.
Based upon the President's joint statement of December 11, 1994 with the leaders of Canada, Mexico and Chile, we have now officially launched the accession negotiations. In announcing the formal commencement of talks in Toronto on June 7, Ambassador Kantor and his counterparts set guidelines for negotiators from the four sides that ensured a successful launch. USTR coordinates the negotiation effort working with an interagency team reflective of the expertise of particular agencies and individuals. We have held four constructive negotiating sessions since the official launching of the talks, but have more work to accomplish before we can conclude an agreement.

The Administration believes it is essential that the United States move forward in a timely and constructive manner successfully to negotiate Chile's accession to the NAFTA and its related agreements. We look forward to working closely with the Congress and our advisors as we progress.

A free trade area with Chile is in our interest as well as Chile's. It will create jobs and economic opportunities in both countries. It will strengthen our relationship with a key friend in the

Americas, and serve as a bridge to forging hemispheric prosperity.

To implement this and other trade agreements, the Administration has been working with key Members of Congress and will continue our efforts to reach agreement on an acceptable fast track authority.

Conclusion

Americans do not fear open and fair competition. All they ask for is a level playing field. This Administration has fought -- and will continue to fight -- to ensure that our trade agreements be "single undertakings" where everyone plays by the same rules. In fact, only with a successful trade agreement strategy will the United States ensure greater economic opportunity for the United States and for our neighbors. We ask for -- we insist on -- a level playing field in trade because it is the right and fair thing to do, and because it is in the best interest of all nations.

As a nation, we are at our best when we reach out and face new challenges. I look forward to working with all of you in the days and months ahead as we strive to foster growth, create jobs and lay the foundation for the 21st century.

Thank you for the opportunity to appear; I would now be happy to answer any questions you may have.

Statement of Alexander F. Watson
Assistant Secretary of State for Inter-American Affairs,
U.S. Department of State,
before the Subcommittees on the Western Hemisphere
and International Economic Policy and Trade,
U.S. House of Representatives,
October 25, 1995

Trade Issues Regarding Chile and Other Latin American Countries in Light of the NAFTA Experience

INTRODUCTION

This is a time of unparalleled progress and hope for our hemisphere. The emergence of Latin America and the Caribbean as solidly democratic and committed to market economics offers the United States unprecedented opportunities: to protect our national security, to pursue our economic interests, and to strengthen cooperation on a whole range of vital transnational interests -- like narcotics, immigration and the environment. These are issues which can have a profound impact on the day-to-day well-being of U.S. citizens.

Last December's Summit of the Americas consolidated the new convergence of values between the U.S. and Latin America, and set out an ambitious action plan. It is no accident that the commitment to negotiate a Free Trade Area of the Americas (FTAA) by the year 2005 was the centerpiece of the Summit. The FTAA caught the imagination of the hemisphere not only because it will bring its participants higher economic growth but also because it symbolizes the new common philosophy of the hemisphere -- of free enterprise, competition and efficiency; of decision-making by markets not governments; of growth and opportunity, rather than centralized government planning. It is also the philosophy which most powerfully supports the profound democratic and social transformations now underway in Latin America.

As President Clinton said when he hosted President Zedillo: "The stronger our trade, the greater the well-being of all of our people. The deeper our cooperation, the better we will be able to fight together our common problems."

LATIN AMERICAN TRADE: IMPORTANT TO U.S. INTERESTS

The U.S. has far more to gain than to lose from a mutual opening of markets in the hemisphere.

Latin America and the Caribbean is already a huge market for the U.S., to which we export almost as much as to the European Union ($89 vs. $96 billion).

It's a fast-growing market. From 1990-1994, U.S. exports to the region increased by $36 billion. During that same period, our exports to the European Union increased by $3 billion, to Japan by $5 billion, to China by $4 billion.

It's a good partner. The commitment to market-based economic reforms remains strong throughout the hemisphere, as shown by the region's reactions to the Mexican peso crisis, which were to deepen reforms, not abandon them. The region's economic fundamentals are growing stronger, with a solid growth outlook, declining inflation, and far greater ability to service debt. More than any other region of the world, it is oriented toward the U.S., buying over 40% of its imports from us. Economic growth and trade liberalization clearly benefit the commercial interests of the U.S.

It has moved far toward open markets, with potential for more. Whereas tariffs of the major Latin American countries averaged close to 50% in 1985, they are now in the teens. Despite this dramatic liberalization, Latin American tariffs are still about four times higher than our own. We clearly have a major interest in moving the liberalization process further.

TRADE LIBERALIZATION: GOOD FOR THE HEMISPHERE

For all of the points noted above, the Administration remains convinced that seeking closer economic ties not only with Mexico, but throughout the hemisphere is in our deepest national interest.

The movement to freer trade is now at a point which requires our active engagement. Latin America has unilaterally lowered its trade barriers to roughly a quarter of what they were ten years ago. Further liberalization, however, almost certainly will take place primarily through international negotiation, rather than by unilateral government decisions.

Latin American and Caribbean countries are moving quickly in forming sub-regional integration arrangements, which now cover virtually every country in the hemisphere. These arrangements generally provide for free trade among their participants, with a common external tariff (typically ranging between 5-20%) to non-participants. Thus, moving toward the larger goal of hemisphere-wide free trade would help to reduce tariffs in Latin American and Caribbean markets.

Remember too, that we are not the only actors in the drama. In addition to the momentum of sub-regional integration, Latin America is forming links outside the hemisphere, with APEC (Asian-Pacific Economic Cooperation) and with the European Union. For example, the EU last month initialed a framework agreement on trade with MERCOSUR, scheduled to be signed before the end of the year. Absent U.S. leadership in structuring a liberalization process, the balance of interest and commitment in Latin America may well start to shift away from us.

NAFTA: IT'S WORKING FOR MEXICO AND FOR THE U.S.

The negotiation of NAFTA marked an important milestone in our relationship with Mexico. It locked in Mexico's commitment to liberal economic reform, increased levels of environmental protection, and ensured that open markets would promote economic growth and employment throughout North America.

Despite continued criticism by some, NAFTA has already proven its worth during Mexico's current economic difficulties. Our overall level of exports is still above pre-NAFTA levels, with every expectation of renewed growth as the Mexican economy rebounds further. U.S. exporters have actually increased their share of the Mexican import market this year from 70% to 73%.

Exports of U.S. goods and services have unparalleled access to Mexico despite Mexico's current recession. Indeed, U.S. exporters' privileged position in the Mexican market has strengthened as Mexico raised tariffs on some imports from third countries. That position will continue to strengthen as Mexico's barriers to its NAFTA partners are phased out in accordance with NAFTA's schedule.

Some have argued that Mexico's current economic problems are the result of NAFTA. That is patently untrue. Mexico's difficulties resulted from a series of political events and its government's macroeconomic policy decisions last year -- not from NAFTA. In fact, the restructuring of the Mexican economy along market-oriented lines, which was reinforced and consolidated by NAFTA, has made it easier for Mexico to rebalance its international accounts and thus more quickly re-establish the conditions for a return to growth.

I know that there has been a lot of concern recently about our trade with Mexico. As Mexico returns to growth and continues to open its market in response to NAFTA, it is reasonable to assume that our exports to Mexico will rebound.

Nor is it reasonable to blame NAFTA for huge job losses in the U.S. economy. Since NAFTA was implemented, overall U.S. employment has increased 4.6 million, and U.S. wages have also increased in real terms.

In sum, NAFTA has been positive for both the U.S. and Mexico. NAFTA not only protects U.S. exporters but ensures continued improvement in their access to the Mexican market. The market-based reforms locked in by NAFTA are restoring

investor confidence in Mexico and have already allowed Mexico to return to the financial markets in seven months, rather than the seven years it took to recover from the 1982 crisis. NAFTA is helping to rebuild the conditions for Mexico's growth, which is strongly in the interest of both Mexico and the U.S.

CHILEAN ACCESSION: GOOD FOR THE U.S. AND THE HEMISPHERE

Chile is an example of the rewards of democratic and market-oriented policies. It has one of the most open trading and investment regimes in the world. International investors have shown their confidence in Chile's prospects by their willingness to invest their money there. Its record of high growth and social innovation is admired and studied throughout the world. Its commitment to human rights is clear and strong.

It was President Bush who first committed the United States to negotiate free trade with Chile during President Aylwin's May 1992 state visit. President Clinton enthusiastically endorsed this policy because of Chile's success not only in economic policy but also in returning to democracy. At the Miami Summit last December President Clinton joined his NAFTA colleagues in formally inviting Chile to join NAFTA. The discussions among the "Four Amigos" to date have been promising. We have exchanged information about each other's trade and investment regimes and have begun to identify focal points for negotiation.

Although passage of fast-track legislation has been delayed, we and our NAFTA partners hope to continue substantive discussions with Chile. Given the strong common beliefs between the U.S. and Chile on both economic and political issues, we expect to continue close cooperation both bilaterally and multilaterally.

Some have questioned why the U.S. should choose Chile as the next NAFTA member, given its relatively small size. First, let me note that while Chile is certainly not a huge market for the U.S., neither is it insignificant. Last year, we sold more to Chile's 14 million people than we did to India's 920 million.

Second, this is a country which is well prepared to enter into and fulfill the commitments of a free trade agreement with the U.S. Its twelve-year record of economic stability and unbroken high growth -- with low unemployment, low inflation, and decreasing poverty -- gives us confidence in its economic policy leadership. The prospect of long-term sustained growth is high given its remarkably high savings and investment rates, and its pioneering commitment to privatization, including its very successful privatization of the social security system.

Finally, in light of Chile's remarkable achievements, Chile's entry into NAFTA would not only demonstrate U.S. support for political and economic reform in the hemisphere, but would also encourage a higher level of trade discipline throughout the hemisphere. Chile is the logical next step as we pursue the Free Trade Area of the Americas.

CONCLUSION

As I noted previously, economic reform and growth in Latin America and the Caribbean are of major importance to the U.S. economy. We have a very broad spectrum of interests, ranging from democracy, to prosperity, to the environment. Almost every problem which confronts U.S. communities today -- crime, drugs, jobs, the environment, to name just a few -- has some transnational aspect. The question before us is not whether to cooperate with our neighbors, but how to structure that cooperation most effectively.

Trade is a crucial part of our relationship with Latin America and the Caribbean. The goal of hemispheric free trade has been accepted by the entire hemisphere, with the unique exception of Cuba. The reforming leaders of the hemisphere have promised their people a better future based on democratic political systems, market-oriented economies, and cooperation with the U.S. Credible movement by the U.S. toward the FTAA is needed to support the political and economic transformations underway in Latin America and the Caribbean. The FTAA will clearly benefit U.S. commercial interests. But it is far more than just a trade initiative. It symbolizes the new relationship between the U.S. and Latin America as equal partners with common values and practical means of cooperation to achieve common goals.

The vision sketched by our leaders in Miami last December was a hemisphere of peace, prosperity and cooperation. Let us move vigorously toward it.

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

**Statement of William E. Barreda,
Deputy Assistant Secretary for International Trade and Investment
U.S. Department of the Treasury
before the Subcommittees on the Western Hemisphere
and International Economic Policy and Trade,
U.S. House of Representatives,
October 25, 1995**

"Trade Issues Regarding Chile and Other Latin American Countries in Light of the NAFTA Experience"

I welcome the opportunity you have given me today to be part of this distinguished panel discussing the NAFTA experience and what it means for Chile's accession.

The excellent statements by Ambassador Shapiro and Assistant Secretary Watson have ably laid out:

-- the reasons why NAFTA continues to be a good deal for the United States; and

-- why we should complete Chile's accession to it.

I do not want to repeat their points. I would like to underscore and expand in a few areas: why NAFTA is good for the United States; Chile's economic performance; Mexico's application of NAFTA's financial services provisions and Chile's financial services market; and the need for a bilateral tax treaty.

NAFTA Is Good for the United States

Mexico's difficulties have led some to question whether NAFTA is in the United States interest. The answer is emphatically yes, the United States is better off with NAFTA than we would have been without it. Specifically:

o Mexico's difficulties were not caused by NAFTA. They were caused by macroeconomic errors.

o During Mexico's economic difficulties, NAFTA protected United States exports and jobs.

-- Mexico cut its tariffs on U.S. exports while it raised them on other countries. This is in sharp contrast to the 1980s.

-- U.S. market share of Mexico's imports increased.

-- U.S. exports this year are still higher than the corresponding period before NAFTA.

o Equally important, Mexico has maintained market-based economic policies and pushed ahead with liberalization despite its difficulties. Again, this is in sharp contrast to the 1980s.

o When Mexico returns to growth, NAFTA will ensure that U.S. exports will share in that growth.

Expanding NAFTA to include Chile is also in the U.S. interest. It will provide our exporters assured access to the Chile market and it will encourage the rest of Latin America to proceed with open market policies-- policies that best ensure their economic growth and our exports to these major markets. I will develop these thoughts.

Chile's Economic Performance

As both Ambassador Shapiro and Assistant Secretary Watson have stated, Chile is indeed an excellent candidate for NAFTA accession. Chilean accession is important for two reasons. First, Chile's economic policies and performance warrant membership. Second, and even more importantly, Chile's example sends a powerful message to other Latin American countries, one which advances United States interests more profoundly than we can hope to achieve through other means.

On the first point, let me share with you a few of the particulars:

o With strong investment and savings and continuing high world copper prices, the Chilean economy is expected to grow by almost 7% in real terms this year.

o Inflation is forecast to fall slightly to 8%, down from last year's nearly 9%.

o Chile's global trade balance returned to its traditional surplus position in 1994. Its 1994 surplus of $660 million is forecast to grow to $2 billion in 1995.

-- The United States had a $1 billion-plus surplus of trade in goods with Chile for the first eight months of 1995, more than double our surplus with Chile for the same period last year. We recorded over $2.3 billion in U.S. exports to Chile for January-August 1995, and nearly $1.4 billion in U.S. imports from Chile.

o In the first quarter of 1995, as financial turmoil roiled

markets elsewhere, total foreign investment inflows remained strong, a good indication of the faith that the private sector has in Chile.

- Chile is a role model of well crafted, firmly implemented macroeconomic policy. Public sector finances have been well-managed as higher social spending under President Frei has been paid for by reduced military expenditures.

- Chile has implemented a pension reform that has made it a high saving country.

- To address infrastructure investment and financing needs, the government has recently allowed private firms to build and operate roads and tunnels. Financing is expected from Chilean pension funds through their purchases of stock of the private firms.

In short, Chile has instituted solid economic policies and is reaping the rewards. Chile serves as a model for its neighbors showing that open markets, a strong public sector budget discipline, and high saving lead to economic growth.

Let me turn to the second reason that Chile's NAFTA accession is so important to the United States, the powerful message it sends to other countries in Latin America and even to other continents.

NAFTA with just Canada and Mexico focuses only on North America and is limited in scope and impact. With the prospect of Chilean accession, NAFTA sets its sights southward and offers other Latin American nations credible inducements to be part of a growing sphere of prosperity.

Other Latin American nations understand that this offer is not without key conditions, namely that of fully open economies and free-market policies. Fostering these conditions in the region is the single most effective way to advance U.S. interests.

Financial Services

Let me turn to an area of special interest for Treasury in NAFTA: its financial services provisions. The United States financial services industry is one of our nation's most competitive and important sectors. NAFTA's financial services provisions have been a real success story.

Mexico

Mexico was a closed market to the United States financial services industry when we began NAFTA negotiations. Under Chapter XIV of NAFTA (Financial Services), Mexico accepted the principles of national treatment, equal competitive opportunity

and most favored nation treatment for financial firms from the United States and Canada. Accordingly:

-- Financial institutions based in the United States and Canada are able to establish wholly owned "foreign financial affiliates" in Mexico, organized as subsidiaries, with the same rights as domestic firms doing the same types of activities.

-- Banks and securities firms, once established, can form financial holding companies, which can in turn establish a broad range of financial subsidiaries.

-- Limited scope finance companies can engage in consumer finance, mortgage lending and credit card banking.

There are transition provisions, which cap the foreign share of the Mexican market until the year 2000.

I am pleased to report that Mexico has lived up to its obligations by licensing new firms. Since April 1994, 107 foreign financial institutions have applied to operate affiliates in Mexico. Of these, 97 applications have received a "Favorable Opinion."

Thus NAFTA succeeded in opening up an important new market for U.S. financial services firms. I should mention as a footnote that the opening to Mexico's financial sector was implemented **after** the onset of Mexico's financial crisis, and did not play any role in the crisis.

Chile

Chile's situation is very different from Mexico's with respect to NAFTA's financial services provisions. Chile is already relatively open to participation by foreign financial institutions.

Eight U.S. banks already operate in Chile through 43 branches. Most U.S. banks have concentrated on corporate lending. A few U.S. banks have significant retail banking businesses. Several have established securities subsidiaries that have no formal connection to their Chilean banking branches.

Chile treats foreign banks the same way that it treats Chilean banks. Chilean investors or foreign banks wishing to enter Chile's banking market must purchase existing banks.

Foreign banks are permitted the same range of activities as domestic banks, including issuance of credit cards, and the offering of ATM services. Foreign banks may fund themselves through deposits as do domestic banks.

Chile's regulatory practices relating to the financial services sector are transparent.

It thus appears that Chile could assume NAFTA's financial services obligations without major difficulty. While Chile is generally open, NAFTA accession would still benefit our financial services industry by providing guaranteed access. The guarantee would go beyond that provided us in the World Trade Organization (WTO). For example, an exciting growth area in Chile has been managing Chile's privatized pension system. U.S. firms are major players in that market, but Chile did not make any WTO market access commitments in the area.

Tax Treaty

Separate from NAFTA accession, but related to it, Treasury intends to negotiate a double taxation treaty with Chile. We see this as a necessary concomitant to NAFTA accession because it will provide reasonable and stable tax rules for bilateral investment, complementing the expansion of trade stimulated by NAFTA accession. We have held preliminary, but encouraging, talks with Chile on this subject.

Conclusion

In closing, Mr. Chairman, I would like to stress that Chile's strong economic performance demonstrates that it is prepared to take on the responsibilities of NAFTA membership and, for all the reasons laid out by Ambassador Shapiro and Assistant Secretary Watson, it is in our economic interest to add Chile to NAFTA. I'll be pleased to try to answer the Committee's questions.

Statement

By Sidney Weintraub
William Simon Chair in Political Economy
Center for Strategic and International Studies

Before Subcommittees on the Western Hemisphere
and International Economic Policy and Trade
Committee on International Relations
U.S House of Representatives

October 25, 1995

The Case for Pursuing a Free Trade Area of the Americas

What follows are ten reasons why the United States should actively encourage the creation of a free-trade area covering the countries of the Western Hemisphere. Many subregional integration agreements already exist, including NAFTA, but the optimum outcome would be a single, hemisphere-wide free-trade area. The Miami Summit of the heads of state and government of the Americas in December 1994 agreed on the year 2005 as the time for completion of negotiations for a Free Trade Areas of the Americas, and this therefore should be the target.

1. *The United States captures 40 percent of the import market of the Americas, about double the U.S. share of import markets of other continents.* What this means is that U.S. exporters, and the U.S. economy as a whole, benefit more from economic growth in the Americas than from growth in any other region. The Americas already account for 40 percent of U.S. merchandise exports, compared with 29 percent for Asia, 24 percent for all of Europe, and 7 percent for the rest of the world (1994 data).

2. *The average U.S. tariff is about 3.5 percent, about one-third the level for Latin America and the Caribbean generally.* Thus, as the countries move gradually toward hemispheric free trade, tariffs against U.S. exports will come down more than U.S tariffs Tariffs are no longer the determining factor in worldwide trade competition, but they are restrictive when they are high. They are not restrictive for most products entering the U.S. market, but they can be for U.S. products entering other markets.

3. *Regional free-trade agreements permit greater progress in removing barriers to U.S. exports than is normally possible in global trade negotiations.* Thus, NAFTA made more progress in opening the Mexican market for U.S.agricultural and service exports, protection of intellectual property, and national treatment for U.S. foreign investment than had years of multilateral negotiation in the GATT. The Uruguay Round then concluded agreements that had eluded previous GATT negotiations in all these fields, undoubtedly stimulated by NAFTA progress. Regionalism cannot replace the more global trade forum, but the two can and do

complement each other

4 *Geographic proximity permits optimal use of production techniques to improve U.S. competitiveness.* World trade increasingly takes place in intermediate products for final assembly in a location close to the ultimate market This does not result in a loss of jobs, but rather greater specialization and competitiveness Thus Japan produces parts of final products elsewhere in Asia and Western Europe increasingly in Eastern Europe U.S. producers do the same on a global basis, but ideally do so in nearby locations like Canada, Mexico, and the Caribbean. Lack of free trade with these countries would not end this co-production, but only shift it to less economical locations, thereby making U.S production less competitive globally. A free-trade area of the Americas would permit this production sharing by all the countries of the hemisphere, particularly in those that afford low-cost transportation.

5. *NAFTA has shown its value in good times and in bad.* Before Mexico's economic debacle, U.S exports there grew rapidly. It is sometimes argued that Mexico is too poor to be a large market for U.S. goods and services, but in fact Mexico last year competed with Japan for second place (after Canada) as a destination for U.S exports. This year, 1995, even with its economic tragedy, Mexico will be our third largest market. In acting to correct its balance-of-payments deficit, Mexico did not impose higher tariffs or import restrictions on U.S. products, as it had done during previous balance-of-payments crises The correction in Mexico's economy is being dealt with by stringent macroeconomic measures, such as generating a budget surplus and tightening the money supply.

6. *The financial rescue package for Mexico mounted by the United States and the International Monetary Fund is working.* The peso has become stable, interest rates in Mexico are declining, inflation has now come down to less than 2 percent a month, and Mexico has been able to borrow in world money markets. This would not have been possible had Mexico defaulted on its government obligations. The economic downturn has been severe -- Mexican gross domestic product will fall by about 5.5 percent this year -- but even here the worst seems to be over. Projections by leading Mexican economists and non-Mexicans who follow the economy closely is that the GDP should rise next year by about 3 percent. This would be a remarkably rapid turnaround to Mexico's worst economic disaster since the Revolution and Civil War ended more than 65 years ago.

7. *Chile is the ideal country to be the first new adherent to NAFTA.* Chile's economy has grown rapidly in recent years; its GDP is projected to rise by 7 percent this year. Its tariff is now a uniform 11 percent and it is prepared to gradually reduce this to zero. Since the plebescite that removed General Pinochet from power, Chile has had two open and democratic presidential elections. Just last week, the military ended its resistance to the imprisonment of a secret service leader convicted of complicity in the assassination of Orlando Letelier in Washington, D C. Chile last year obtained 27 percent of its imports from NAFTA countries. I am horrified that despite promises by two U.S presidents, the United States has been unable to make good on its desire to complete negotiations for Chile's accession to NAFTA. I am not here castigating either the

Congress or the Executive, but rather both for an inability to work out a reasonable arrangement for completing negotiations and approving Chile's accession.

8. *The excitement that pervaded the hemisphere when President Bush proposed crafting a free-trade area from Alaska to Tierra del Fuego has largely dissipated.* The reason is that, other than convening hemispheric conferences, the United States has demonstrated its inability to make any progress in achieving this goal. What we are witnessing, instead, is the atomization of the hemisphere and the creation of numerous preferential trading areas that exclude the United States. Trade is increasing in the hemisphere -- between Argentina and Brazil, between Colombia and Venezuela, to give just two examples -- but the United States is not getting the share it could. The countries of the hemisphere are waiting for U.S. leadership, but they are not getting it.

9. *Meanwhile, the European Union continues to make progress in expanding its trading region and moves toward regional trading agreements are taking hold in Asia.* The EU has even made overtures for a trade agreement with MERCOSUR, the common market of the south consisting of Argentina, Brazil, Paraguay, and Uruguay. Chile and Bolivia are negotiating agreements with MERCOSUR. The odd country out is the United States. We are not leading; we are lagging.

10. *Finally, a political point. This is our hemisphere and if we can't show leadership here, where can we?* We have everything to gain, but still we delay. I am certain that one day we will get to hemispheric free trade because it makes economic sense for us and for the rest of the hemisphere. But time is passing us by.

UNITED STATES

BUSINESS AND INDUSTRIAL COUNCIL

Testimony before the

House Committee on International Relations

Subcommittees on the Western Hemisphere and on International Economic Policy and Trade

by Kevin L. Kearns
United States Business and Industrial Council
President

October 25, 1995

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Kevin L. Kearns
U.S. Business and Industrial Council

October 25, 1995

I am Kevin L. Kearns, President of the U.S. Business and Industrial Council. The Council was founded in 1933 to represent the interests of medium-sized, family-owned and run American companies, especially in the manufacturing sector. Historically, the interests of these companies have sometimes differed from large scale enterprises. In the last fifteen years, with the advent of a more globalized economy and an increasingly open U.S. market, those differences have grown significantly.

The members of the Council are of the firm belief that the purpose of the American economy is to provide a decent job and growing standard of living for all Americans. Today, we believe that the economy is being run for the benefit of the executives and shareholders of American multinational corporations, whose corporate interests now differ significantly not only from small and mid-sized businesses, but also from the U.S. national interest. To update the well-known aphorism, "What's good for General Motors is probably bad for the rest of America."

The U.S. marketplace has become globalized as a result of the U.S. government's blind adherence to free trade ideology. It is the only marketplace in the world in this state of advanced globalization. The inability of government officials to conduct a trade policy that is in the American interest has been apparent for many years, as foreign goods have flooded U.S. markets, taking significant market share, while key markets abroad in Japan, China, and European countries are protected through tariffs, quotas, restriction on investment, and non-tariff barriers to the importation of American goods. Year after year, we continue to try to negotiate bilaterally for market access for our goods and, year after year, our trading partners stall and equivocate. While our exports have increased, our imports have increased faster. Free trade proponents only count exports, however, and never mention imports. It is as if they were to try to run their companies only by looking at the income side of the ledger and not at their expenses. The bottom line is, of course, always a net figure, income minus expenses. So it should be with imports and exports. Unfortunately, the never-mentioned net figure is a huge minus for the United States as a whole and for American working men and woman in particular.

The incompetence of American trade officials and the inadequacy of their free trade policies has deprived American business of the profits and economies of scale that full access to foreign markets would bring. Instead, American multinational corporations try to make up for the resulting loss of competitiveness by chasing cheap labor around the world. They move capital and relocate factories at will, in order to sell their products more competitively here in their home market. CEOs of large corporations commute from their privileged communities to gleaming corporate headquarters and lay-off thousands of people whom they have never met and whose names they don't know – all in the name of increased efficiency, greater productivity, and increased profits. Unfortunately, they don't have to live with the social consequences of their business decisions. These are someone else's problem.

Medium-sized and small American companies have a different perspective. The owner-managers work in the business along side their employees, whose names and families they know. They live in the same communities, attend the same churches and synagogues, and belong to the same organizations. Their kids and grandkids go to the same schools as do their employees kids. When they are forced to contract their businesses, they know who is being laid off. They see the

results of lay-offs directly. They know what it means to a community to have unemployed friends and neighbors. They sometimes see marriages break up, or drug abuse, or kids acting up in school because things aren't right at home. These are the human faces of efficiency, and downsizing, and increased international competition. These are the social consequences of unbridled free trade, unmeasured, and like imports, unmentioned by neoclassical economists and free trade proponents.

The cumulative impact of our failed free trade policies has been a staggering $1.2 trillion trade deficit in manufactured goods over the last fifteen years. The economic impact has been the loss of millions of high-paying manufacturing jobs, and it should be pointed out, the billions of dollars in tax revenues that they used to generate. In 1950, one in three Americans held a manufacturing job; now the figure is about one in seven, and continues to decline. The service sector today stands roughly where the manufacturing sector stood in 1950, employing one in three Americans, but there is a big difference: On average, service sector wages are about three quarters of those of manufacturing. In short, a service sector job is generally not a substitute for a manufacturing job, as it brings a lower standard of living.

However, all of the job creation in the last twelve years has been in the service sector, which is by and large not involved in international trade. There has been no increase in net jobs in traded industries during this period. The Fortune 500 have not created one net new job in the United States in years. U.S. multinationals have taken up corporate downsizing with a vengeance, all the while continuing to relocating manufacturing operations overseas. (Many firms are also beginning to move their white collar clerical operations off shore to English language countries, such as the Philippines, India and Jamaica.)

The ability to move capital and technology around the world rapidly has had a very negative impact on American wages. Between the mid 1950s and the early 1970s, real wages rose for all American workers. Since the early 1970's, real wages have fallen significantly. The bottom four quintiles of Americans or eighty percent of Americans, have seen their incomes decline in real terms. Even the top quintile, the elite with the most education, has seen the rate of its income growth cut in half when the period 1976 - 1994 is compared to 1956 - 1976.

There is a direct relationship between successive rounds of trade liberalization, the opening of the American market, the decline of manufacturing, and the decline in real wages. Perhaps the most surprising result of international competition in the American marketplace has been the de-linkage of wages from increases in productivity. During the period 1956-1972, wages rose as workers became increasingly productive and the market compensated them accordingly. From 1972 onward, the productivity of the American worker has continued to rise. In fact, in the last several years it has skyrocketed. But real wages have continued to decline.

Why has this phenomenon occurred? Because American workers are now competing not merely with other American workers across the state or across the country. They are competing with workers from around the world, all of whom will gladly do the same job for much less pay. Partially, this labor competition is the result of falling trade barriers in the industrialized world. But the greater part comes as a result of political decisions by governments that had previously barred their workers

from taking part in the world economy. Several billion individuals from China, India, Russia and the former Soviet states, Vietnam, etc. have entered the world marketplace to sell their labor. The effect on American wages has been disastrous.

The social impact on the United States has also been widespread and often devastating. A single wage earner has been unable to support a family for some years now. To try to keep families afloat, millions of wives have joined the work force over the last twenty years. The stress on individuals, marriages, children, schools, and communities is not something that economists measure as a result of the globalization of the American economy, but Americans know both intuitively and from statistics on various subjects such as crime, SAT scores, out-of-wedlock births, and divorce that our social cohesion has suffered greatly as millions tumble down the wage and job scale.

NAFTA was the response of American multinational corporations to their inability to compete in the American market against their subsidized and protected foreign rivals. It was also the political response of government officials and politicians, whose pet free trade theories were not delivering for average Americans. Somehow, more of a failed theory was supposed to produce different results.

NAFTA, with its putative benefits in the form of increased exports to Mexico and, from newly established American factories in Mexico, to the rest of the world was supposed to be the solution. NAFTA was supposed to address the problems of competitiveness of American firms and to provide American working people with more and better jobs. It was also supposed to improve the lot of Mexican workers and create a large middle class in Mexico, which in turn would absorb American consumer goods. NAFTA was supposed to be a fantastic win-win situation for businesses and workers on both sides of the border.

As the trade, wage, productivity, and employment statistics show, NAFTA is an abysmal failure. Nothing could be further from the truth than the many allegations about the benefits of NAFTA made by its proponents. Nothing could be further from the truth than their description of Mexico as a politically stable, first-world country with a democratic system of government and an economy system in which all citizens had a stake. The Chiapas rebellion, the assassination of the ruling party's presidential candidate, the implication of former President Salinas's family in another high-level assassination, a large and growing drug trade with the United States (DEA now estimates that 75 percent of the illegal drugs in this country come through Mexico), all these facts fly in the face of the political claims made by NAFTA proponents.

Their economic claims were also greatly overstated. The United States has gone from a $5.7 billion trade surplus in 1992 to a projected deficit of $20 billion in 1995. The Mexican government is approving applications for new factories at the rate of two or three a day. These factories are being set up along the border to service the American market with jobs that were previously done by Americans now being performed by Mexicans. Two hundred thousand manufacturing jobs have been lost so far this year. Our skyrocketing deficit with Mexican is in goods that we make here in the United States. Clearly, American workers are being displaced.

Mexico has not been a winner either. The Mexican economy began to experience an influx of so-called hot portfolio money during the NAFTA negotiations. These funds were speculate in nature and were free to leave as quickly as they came, which they did when the peso crisis occurred. During the year preceding the peso crisis and devaluation, the Mexican government spent $20 billion, almost all the country's foreign reserves to artificially prop up the peso. This action was undertaken to create the illusion of a stable prosperous Mexico for the American audience. Please note that Mexico did not devalue the peso, the market did. The Mexican government had been trying to over ride market forces for four years but failed when it ran out of foreign exchange.

As a result the American taxpayer got stuck with a $50 billion tab for the bailout. The economic ramifications were bad enough, but the political ramifications were worse. The Clinton Administration and the Congressional leadership simply went around the American people and their elected representatives when objections arose in Congress to bailing out the Mexican elite and Wall Street investors. Our democratic system was shelved in order to bailout and preserve a corrupt Mexican elite and Wall Street financiers who had been making huge profits on their Mexican investments.

Thousands of small businesses failed in Mexico, as credit dried up and the economy contracted. One million Mexican workers lost their jobs. American retail operations in Mexico, which had opened with such fanfare a year before, closed their doors. The claim that there was going to be a large increase in exports of American consumer goods was shown to be an illusion as the wages and purchasing power of Mexican workers eroded substantially in the face of runaway inflation. This situation is producing substantial hardship on almost all Mexican families, with the exception of the privileged few.

The solution to the crisis is for Mexico to calm its foreign exchange and securities markets with vastly increased exports to the United States, while curbing imports drastically. Mexico's other major trading partners are still running surpluses with Mexico. So it is the United States that is bearing the brunt of the crisis. For these and many more reasons, to numerous to list here, NAFTA in fact has turned out to be very different from NAFTA in theory. Everything that we have learned so far indicates that we should not extend the NAFTA arrangement to any other country unless we can make it work in the interests of all Americans.

Let me turn specifically to the question of Chile's accession to NAFTA. I recently spent one week in Chile at the invitation of CONUPIA, the federation of small and medium-sized Chilean businesses. I had extensive conversations with Chilean businessmen, trade unions, agricultural organizations, and environmentalists. I testified before the committee of the Chilean Senate with jurisdiction over NAFTA. I talked to representatives of the American Chamber's new NAFTA office and met with economists at the Untied Nations Trade organization, headquartered in Santiago. I believe that I the opinions of all points of view on the issue of Chilean accession to NAFTA.

Kevin L. Kearns
U.S. Business and Industrial Council

October 25, 1995

There are four main areas of benefit for Chile expected by NAFTA proponents if Chile joins NAFTA:

1. Increased access to a broader market;
2. Increased foreign investment;
3. More intense competition in the home market; and
4. Prestige in being linked to the United States.

It is my opinion that these alleged benefits do not stand up under more rigorous analysis. U.S. duties on Chilean products are already extremely low. An expanded NAFTA would not make much of a difference to Chile's exporting industries. However, it must be remembered that 86 percent of Chile's exports are natural resources. It exports relatively small numbers of manufactured goods, which are not of international quality. These goods are exported to other Latin countries where the competition is not great. Chilean manufacturers are in no way ready to go head-to-head with North American manufacturers. They describe themselves as twenty years behind the times in technology and management techniques, and always short of capital, which is generally directed to the large scale enterprises engaged in harvesting natural resources.

Foreign direct investment in Chile has been up substantially in recent years. Last year the figure was $4 billion and this year is running ahead of 1994. Increased foreign investment is likely to continue under NAFTA, but the trend will almost certainly follow that of recent years, where almost all FDI goes into natural resources, the vast majority into copper mining. There are several problems with this trend. Chile's spectacular environment is already being severely degraded by pollution from mining and the toxins of modern agribusiness. It rivers are polluted and its ground water is becoming polluted. Over fishing has already caused the extinction of one species of fish and the general depletion of fishing stocks.

The application of significant new amounts of capital to increase the yields of Chile mines, farms, fisheries, and forests will likely result in further environmental degradation and perhaps the additional depletion of particular resources. Further, the high-tech harvesting of land and sea produces few new jobs as it is technology and not labor intensive.

Ironically, increased investment is likely to cause a significant decrease in the number of jobs in agriculture and fishing. As agriculture becomes technology intensive, thousands of Chile's 600,000 agricultural workers will be forced off the land, only to create new slums on the fringes of Chile's cities. The 250,000 small farm owners are also likely to disappear altogether in competition with U.S. and Canadian farmers. The Chilean government estimates that at least half of the farmers will be displaced. The same is true of the fishermen who own their own boats. Already thousands have been idled by over fishing and displaced by the large factory ships, which very efficiently vacuum the sea. The fishermen who are able to remain in business, work much longer and harder. It often takes them three to four times as long to catch the same number of fish that they did several years ago. There is, of course, a severe impact on traditional ways of life and the cohesion of long-standing communities,

especially on families, that does not show up in the direct investment statistics. The consequences of the efficiency and technology of increased investment are not merely that jobs are disappearing but that traditional ways of life are disappearing and large numbers of people are deracinated.

Where will these displaced workers go? The theory is that the market will create opportunities, set a price on their labor, and employ and pay them accordingly. The reality is that there are unlikely to be any jobs which will provide Chilean farmers and fishermen the same standard of living and a cohesive way of life.

The alleged benefit number three – more profound competition in the internal market, which will lead to increases in efficiency and productivity – will very likely come true as goods from multinational factories operating in Mexico flood into the Chilean market to compete with the output of Chilean factories. The Chileans rightly pride themselves on the fact that their market has been liberalized and rationalized over the last twenty years. But in the opinion of the many businessmen that I talked to during my recent trip, the small and medium-sized business sector is not ready to compete with multinationals nor is it ready to absorb displaced agricultural workers and fisherman.

In fact, consolidation in that sector has already spawned a phenomenon known as the micro-firm, i.e. very small organizations of one to three people who formerly worked for larger economic units and are now scrapping for a living. While NAFTA proponents made the false claim that the agreement would spur job creation in Mexico and enlarge the middle class through increased investment, not even the most ardent Chilean proponents make such a claim for Chile under NAFTA. And Chilean businessmen from small and medium-sized organizations believe that there will be significant numbers of jobs lost due to increased competition with off-shore firms. Already they are having difficulty with goods from Colombia and Bolivia, where they say manufacturers benefit from government subsidies.

It must constantly be remembered that Chile is a very small country, 15 million people. While the unemployment rate is a relatively low 5.5 percent, there is significant under employment and approximately 43 percent of the workforce is being paid poverty wages. Income distribution is highly skewed toward the rich with the top 20 percent of the population collecting 56 percent of the wealth and the bottom one-fifth a low 5.1 percent. The NAFTA argument in regard to Mexico that there was already a large and growing middle class market for American consumer goods simply cannot be applied to Chile.

Thus the prospects for Chile's internal market are limited even with the six percent growth rates of recent years. It is uneconomic for foreign multinationals to set up manufacturing plants in this small, geographically remote country. The Chilean market for manufactured goods can be serviced quite well from American and foreign multinational factories already operating in the United States, Canada, and Mexico. When Chile is mentioned as a gateway to Mercursor or other Latin markets, the reference is only to the precedent of signing Chile up for NAFTA, not to the possibility of Chile's becoming a manufacturing base to export to them. That would be better done from either Mexico's new multinational factories or from new factories in a larger Latin market, like Brazil.

In addition, Chile's wages, while low compared to the United States, are nonetheless higher than Mexico's. It is shocking to Chileans to point out that there are currently 15 million unemployed workers in Mexico, a figure equivalent to the entire population of Chile. That means that as the Chilean economy continues to grow, which it can do very nicely without NAFTA, Chilean labor will become even more uncompetitive with Mexican labor.

The likely consequence of NAFTA accession for the indigenous Chilean manufacturing sector is that it will be subjected to intense competition, which will result in a significant shake-out of Chilean firms with resulting unemployment. Chile will have a very efficient economy, but also a large employment and underemployment problem. As average Chileans tumble down the wage and job scale, they can take scant comfort that exactly the same thing is happening to average American workers, with their declining real wages – all courtesy of free rade theories.

The consumer, the central character in free trade theory, can only benefit from access to higher quality, lower priced goods, and thus an improved standard of living, if his own wages at least remain stable. However, when much of the population is experiencing a decline in real incomes, the benefits of free trade become an illusion. And if the consumer loses his job altogether, then it doesn't matter how inexpensive or how high quality the goods are. One must first be a producer before one can be a consumer.

The political implications for both Chile and the United States are frightening. Families and individuals without meaningful work and who are unable to feed themselves are likely to become increasingly dissatisfied with an economic and political system in which they do not have a stake. Free trade produces efficiencies, but efficiency should not be the goal of a national economy. As I mentioned at the outset, the businessmen and women of the United States Business and Industrial Council believe that the proper goal of a national economy is to produce a society in which all its citizens have a stake, through meaningful work and a growing standard of living.

Given the experience with NAFTA to date, that is that it is clearly a lose-lose proposition for both the Untied States and Mexico, I wonder what the rush is to expand it. Chile's economy is likely to do very well without NAFTA. Six percent growth is very healthy. Why push the Chilean economy into uncharted territory when it is already doing so well?

The United States has various valid objectives in negotiating with Chile to protect the economic interests of American companies. These include:

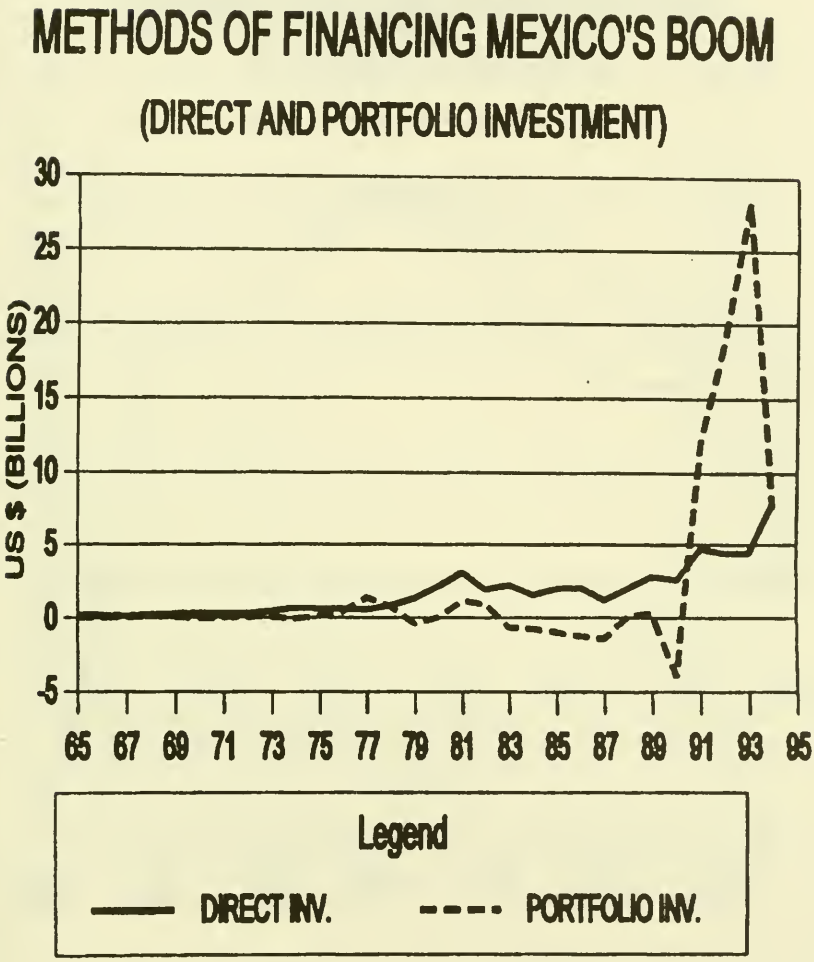
1. Halting software piracy;
2. Protecting intellectual property through increased patent protection, especially in the pharmaceutical area;
3. Removing the various taxes which discriminate against American automobiles;
4. Increasing access for American poultry, fruit and vegetables in Chile; and
5. Eliminating discriminatory taxation on imported U.S. whiskey.

These objectives can be met through bilateral negotiations and do not require NAFTA accession. In fact, accomplishment of these objectives should be a prerequisite for a closer economic union between the United States and Chile should that be indicated at some future time.

In closing, I would simply like to reiterate that NAFTA is not working, and thus should not be expanded. Rather an excellent case can be made to undo the harm that NAFTA is causing rather than to extend it. NAFTA is accelerating job loss in the United States and lowering the standard of living of American workers, especially those who are being replaced directly by cheaper Mexican labor. A million Mexican workers have lost their jobs and thousands of small businesses have failed as a result of NAFTA. Mexico is not the stable, first world country that NAFTA proponents claimed, but an unstable and corrupt country, through no fault of the average Mexican citizen, but of the elites. NAFTA did not make Mexico an export platform from which U.S. multinationals could service the world, rather it was a re-export platform right back to the United States – which means that our chief export to Mexico is good American jobs.

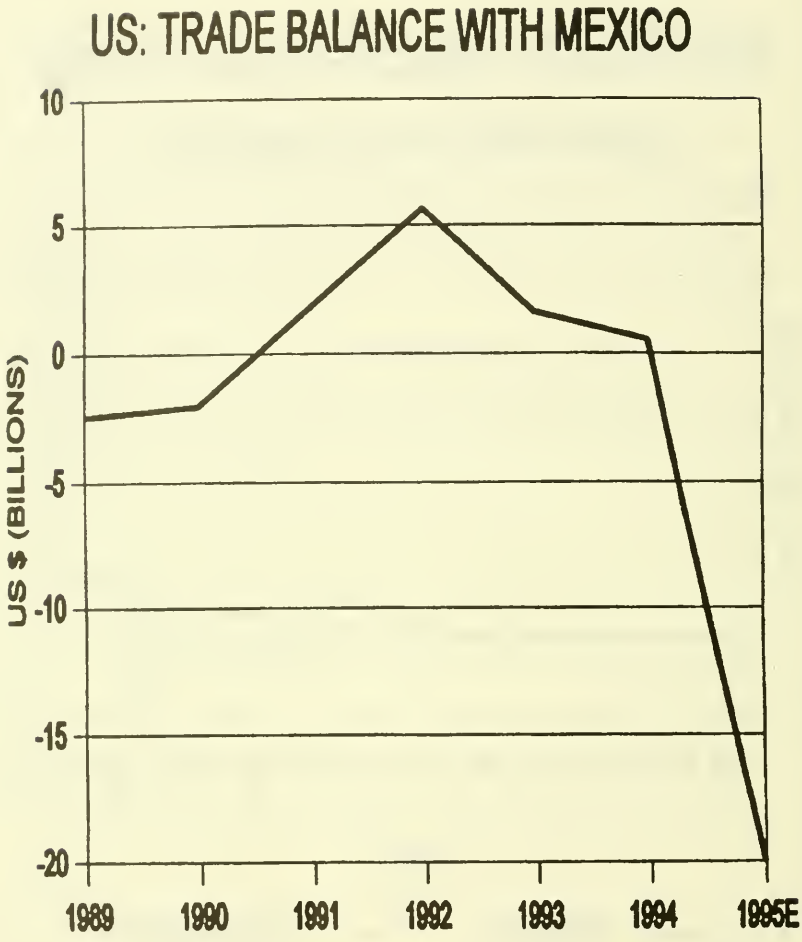
If Chile accedes to NAFTA, then Chile will likely become the first "beneficiary" of the Mexican export platform at great detriment to its own manufacturing sector. Unfortunately, in pushing to join NAFTA, Chile is rushing ahead to the past. There will be no manufacturing or high-tech gains for Chile under NAFTA, merely an increase in the centuries old exploitation of its natural resources. Traditional ways of life will disappear in response to the modern dictates of technology and efficiency, and the likelihood is that instead of increasing its political stability NAFTA will have exactly the opposite consequence.

Chart 1 – Kevin L. Kearns, President, U.S. Business and Industrial Council



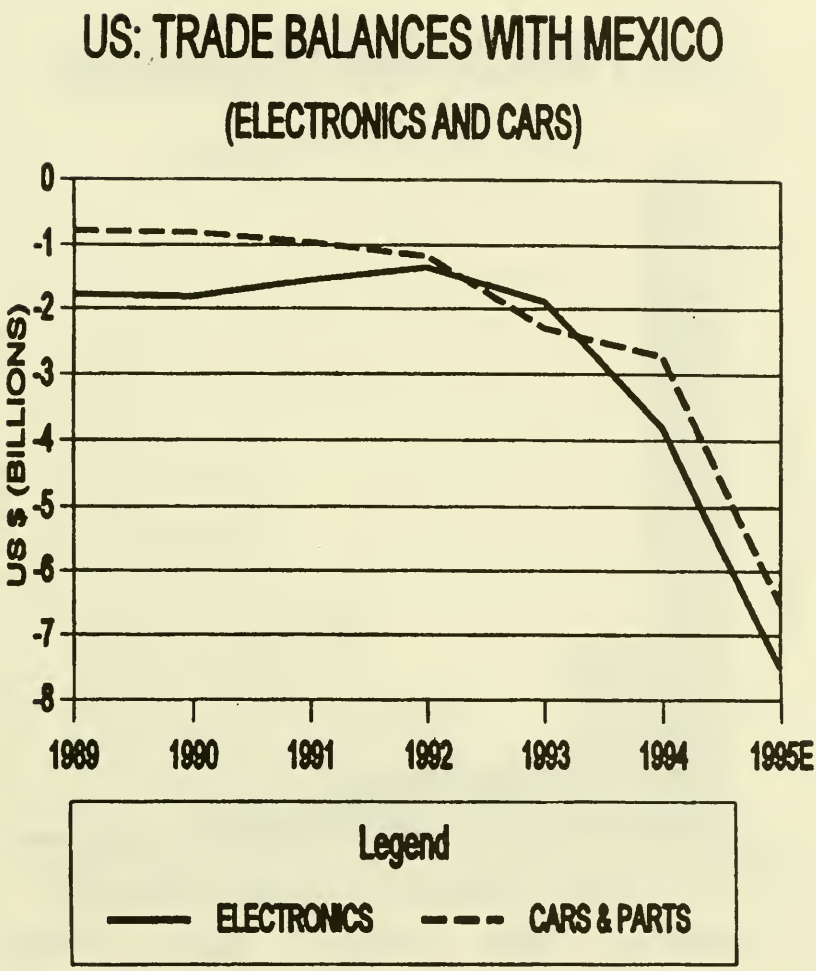
Source: *International Monetary Fund.*

Chart 2 – Kevin L. Kearns, President, U.S. Business and Industrial Council



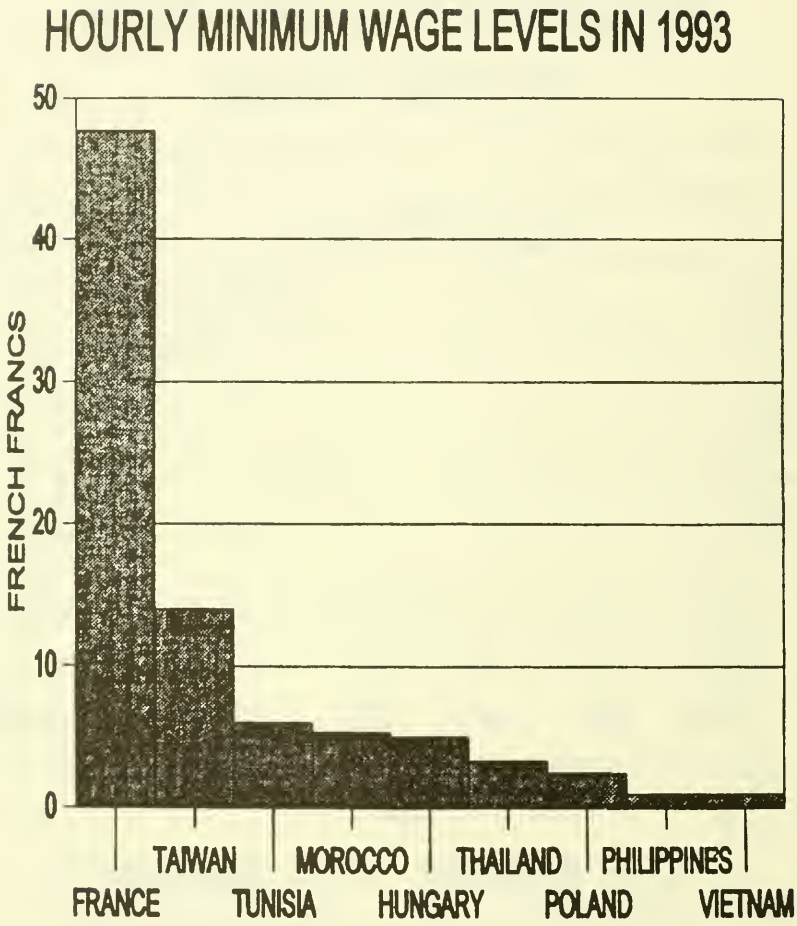
Source: *US Department of Commerce and MBG Information Services.*

Chart 3 – Kevin L. Kearns, President, U.S. Business and Industrial Council



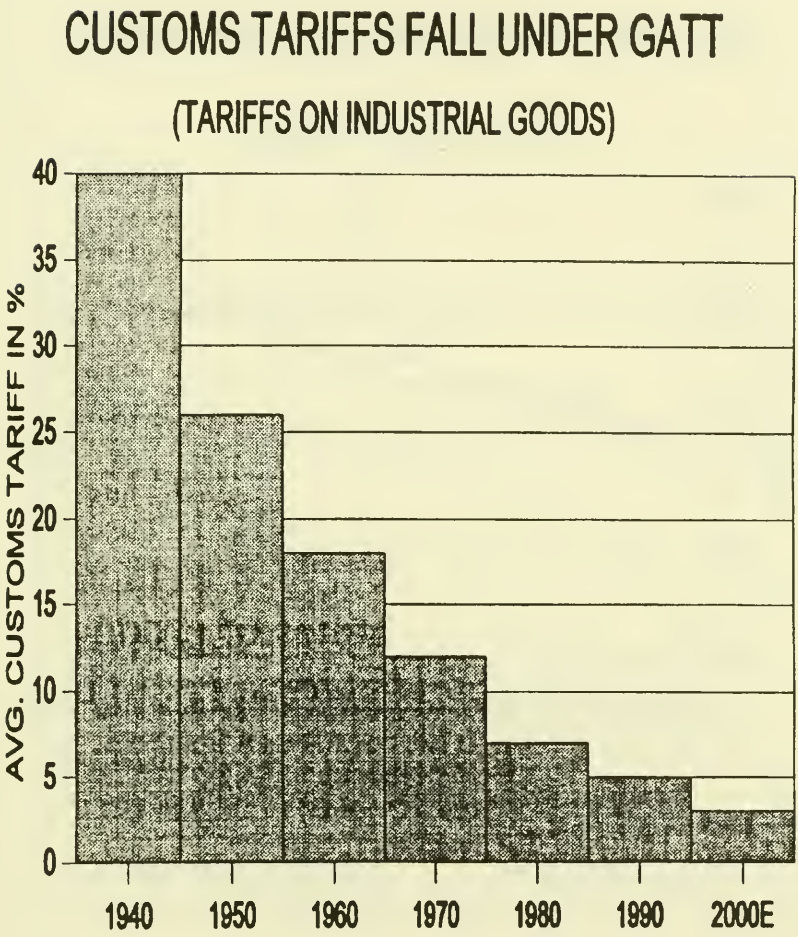
Source: *US Department of Commerce and MBG Information Services.*

Chart 4 – Kevin L. Kearns, President, U.S. Business and Industrial Council



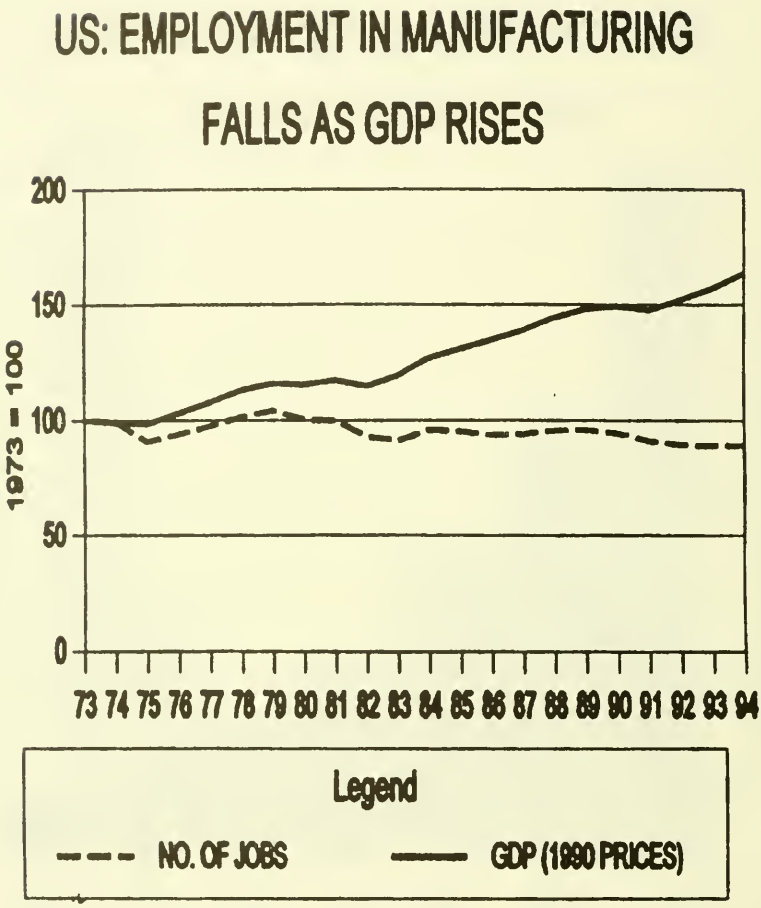
Source: *French Senate Finance Committee and Direction des Relations Economiques Extérieures.*

Chart 5 – Kevin L. Kearns, President, U.S. Business and Industrial Council



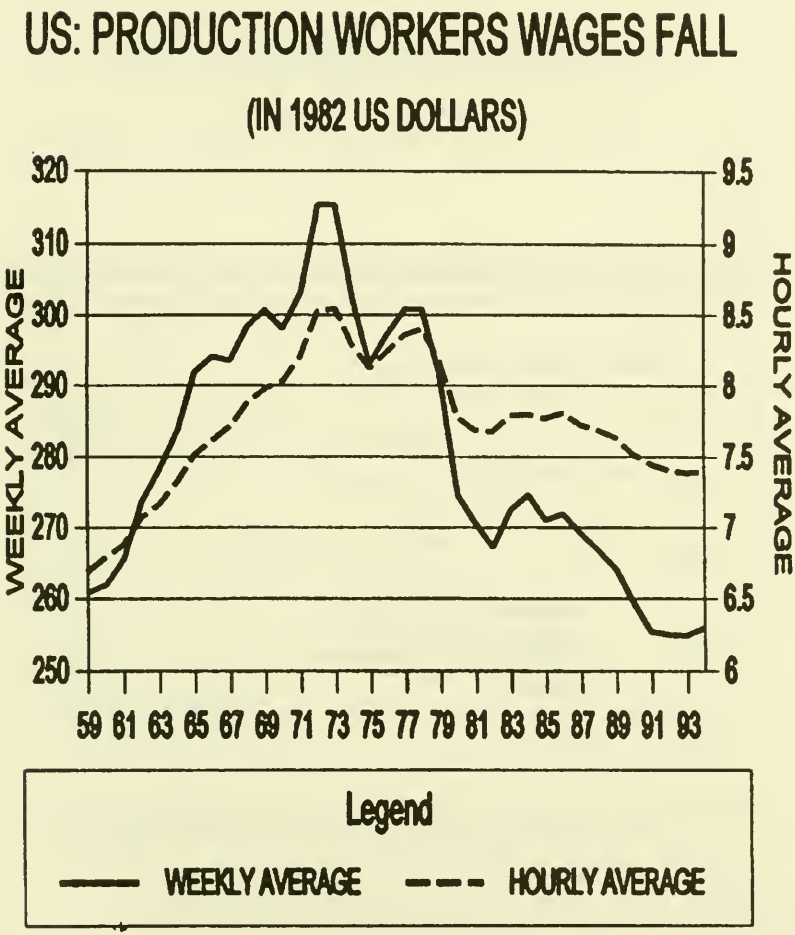
Source: *GATT Secretariat.*

Chart 6 – Kevin L. Kearns, President, U.S. Business and Industrial Council



Source: *US Bureau of Labor Statistics, and the International Monetary Fund.*

Chart 7 – Kevin L. Kearns, President, U.S. Business and Industrial Council



Source: *US Department of Labor, Bureau of Labor Statistics.*

Chart 8 – Kevin L. Kearns, President, U.S. Business and Industrial Council

U.S. NET EXPORTS AND SUCCESSIVE ROUNDS OF TRADE "LIBERALIZATION"

Repeated Promises of Improved U.S. Net Exports Have Not Materialized

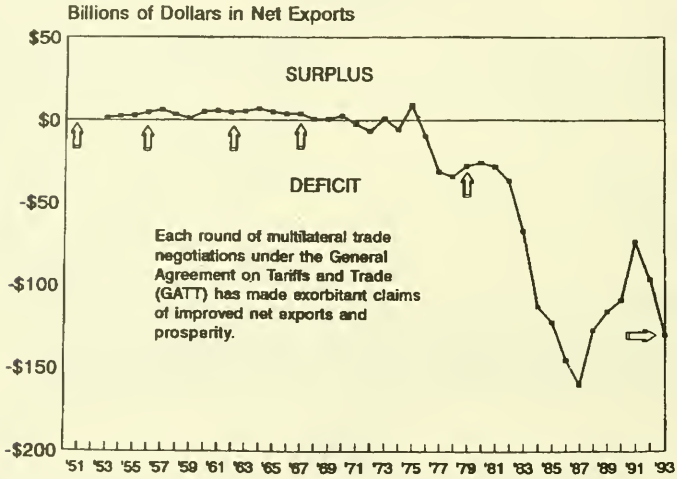
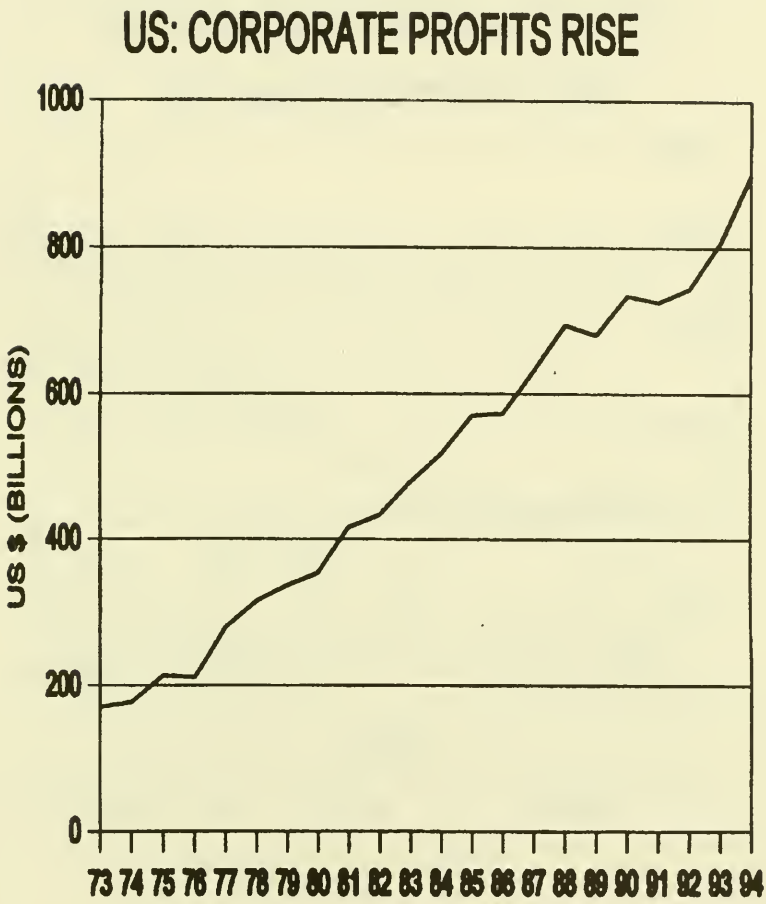
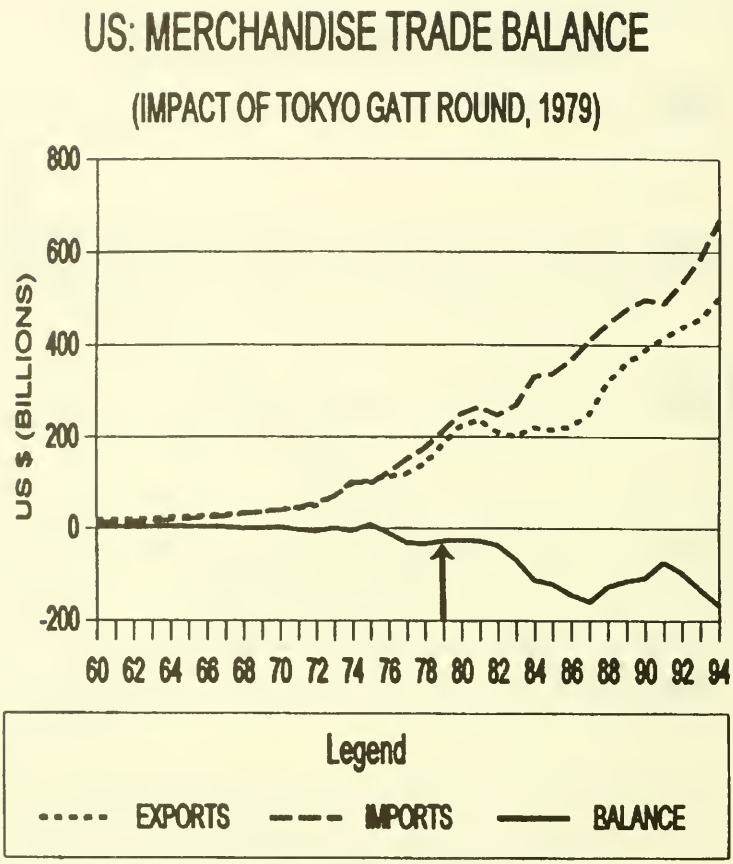


Chart 9 – Kevin L. Kearns, President, U.S. Business and Industrial Council



Source: ***Organization for Economic Cooperation and Development.***

Chart 10 – Kevin L. Kearns, President, U.S. Business and Industrial Council

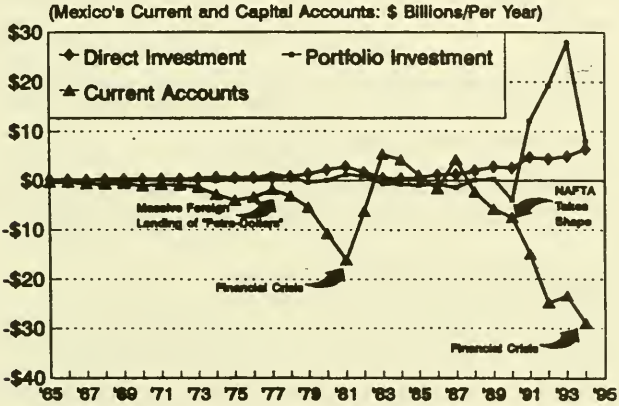


Source: *US Department of Commerce.*

Chart 11 – Kevin L. Kearns, President, U.S. Business and Industrial Council

CAPITAL BEGAN TO POUR INTO MEXICO IN 1991

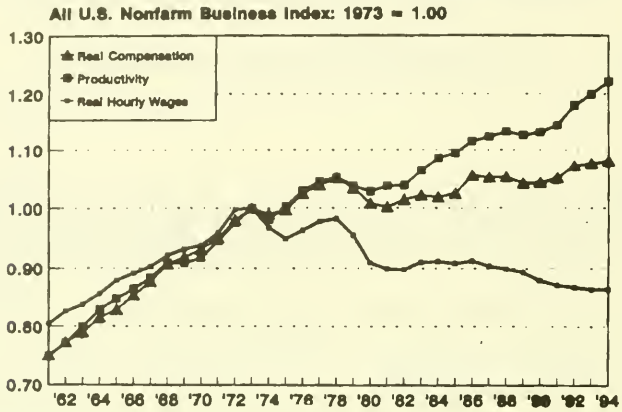
It Stopped in April, 1994 As World Capital Markets Tightened



International Monetary Fund and MBG Information Services (202) 544-6490

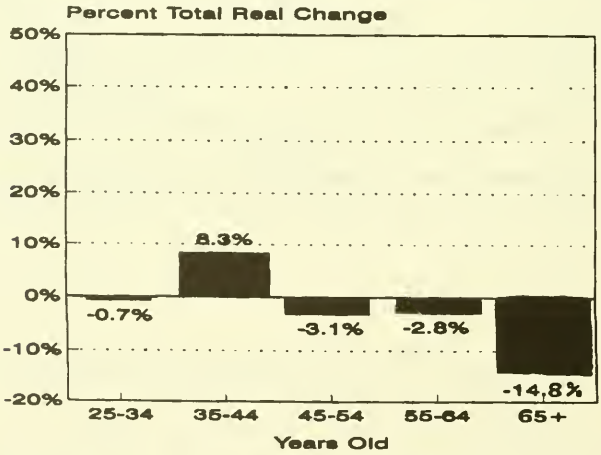
Chart 12 – Kevin L. Kearns, President, U.S. Business and Industrial Council

WAGES ARE FALLING AND COMPENSATION IS STAGNANT IN U.S. BUSINESS
The Virtual Identity Between Wage and Productivity Growth Has Been Shattered



MBG Information Services and U.S. Department of Labor, BLS.

MEN COMPLETING FIVE OR MORE YEARS OF COLLEGE
Real Yearly Wages & Salaries: 1974 and 1990



MBG Information Services and U.S. Bureau of the Census

Chart 13 -- Kevin L. Kearns, President, U.S. Business and Industrial Council

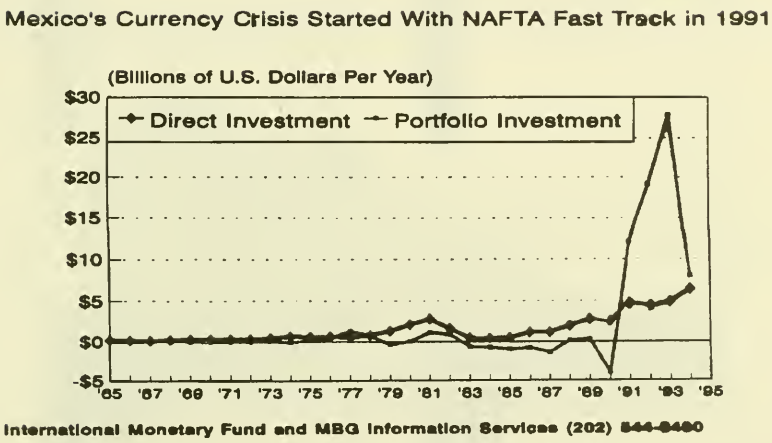
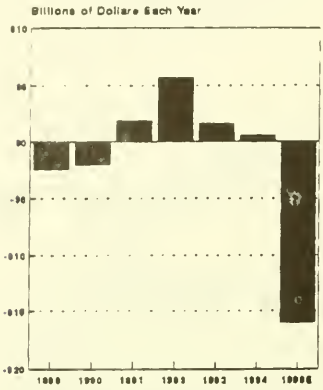


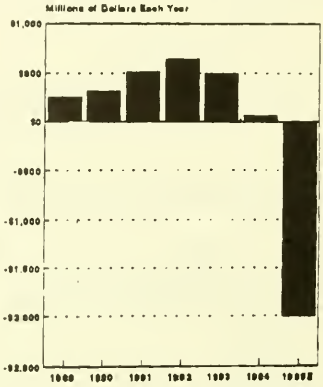
Chart 14 – Kevin L. Kearns, President, U.S. Business and Industrial Council

MEXICO'S HIGH TECH TRADE SUCCESS IS U.S. LOSS

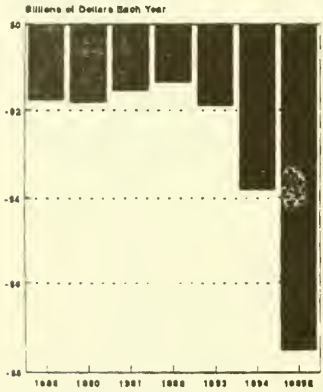
U.S. Total Trade Balance With Mexico



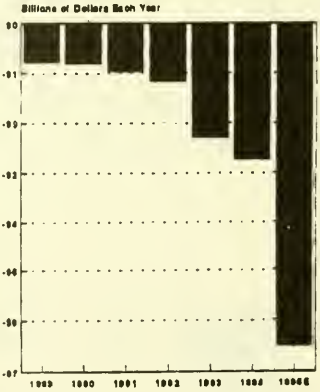
U.S. Trade Balance With Mexico in Scientific Instruments



U.S. Trade Balance With Mexico in Electronic Equipment



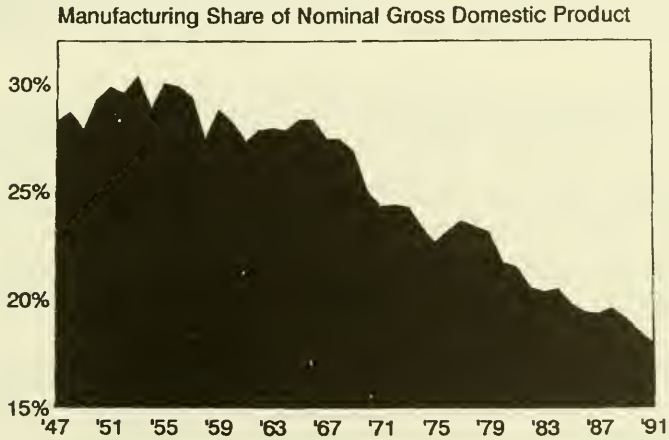
U.S. Trade Balance With Mexico in Automobiles and Parts



U.S. Department of Commerce and MBQ Information Services (202) 944-6480

Chart 15 – Kevin L. Kearns, President, U.S. Business and Industrial Council

THE DECLINING SHARE OF MANUFACTURING IN THE U.S. ECONOMY
International Trade Is Driving the Economy to Shift Out of Productive Traded Industries
And Into Less Productive, Non-Traded Services Sectors



Department of Commerce, BEA.

UNITED STATES

BUSINESS AND INDUSTRIAL COUNCIL

Kevin L. Kearns is the President of both the United States Business and Industrial Council, and its affiliate, the United States Business and Industrial Council Educational Foundation. The Council is a national organization representing the interests of 1,000 companies from 44 states before the U.S. Congress and the Executive Branch. The Foundation is the research arm of the Council and in addition runs college speakers and student newspaper assistance programs. Mr. Kearns also serves as the Chairman for the Business Coalition for Affordable Health Care, a group organized by the Council to promote free-market health care reforms.

Prior to joining the Council and Foundation, Mr. Kearns was a Senior Fellow at the Manufacturing Policy Project and the Economic Strategy Institute in Washington, D.C., where he specialized in business, international trade, and American industrial competitiveness issues. From 1977-90, Mr. Kearns was a career Foreign Service Officer holding a wide variety of positions both in Washington and abroad. His last position with State was Director, Office of Strategic Trade Policy, where he was responsible for overseeing U.S. government policy on commercial use of space, satellites, supercomputers, export controls, and missile non-proliferation.

During his time with the State Department, Mr. Kearns was posted in Frankfurt, Bonn, Seoul and Tokyo. He served in diverse positions, including economic and commercial officer, political officer, Ambassador's aide, and Defense Exchange Officer at the Pentagon. In Tokyo he was the Deputy Chief, Mutual Defense Assistance Office, and was deeply involved in the FSX fighter plane negotiations. While serving in Washington, Mr. Kearns was a political-military officer overseeing U.S. security assistance programs to Latin America. He participated in the Grenada rescue operation in 1981 and spent significant time in El Salvador during the civil war there. While serving as Philippine desk officer, he was sent to Mindanao as an election observer during the Marcos-Aquino presidential election of 1986.

Mr. Kearns received a State Department fellowship to serve as a professional staff member of the Senate Foreign Relations Committee, where he played a significant role in the FSX and Chinese-launch-of-U.S.-satellites debates. Before joining State, Mr. Kearns was campaign manager and then legislative counsel to N.Y. State Senator Sheldon Farber.

Mr. Kearns is a regular contributor to and is frequently quoted in such publications as The Washington Post, The New York Times, The Wall Street Journal, The Journal of Commerce, The Christian Science Monitor, International Business Magazine, the Asahi Monthly and Bunkei Shinju on issues associated with competitiveness, business, economic, and high-technology issues, as well as U.S.-Japan relations. He has testified before numerous Congressional committees including the Senate's Foreign Relations, Finance, and Judiciary Committees and the House's Foreign Affairs, Budget, and Energy and Commerce Committees. Television appearances include ABC's Prime Time Live, the CBS Evening News, the PBS series Techno-Politics, CNBC's Financial News, American Interests with Morton Kondracke, and CNN's Headline News. Mr. Kearns is also a frequent guest on business-related subjects on talk radio shows across the country.

A native of New York City, Mr. Kearns holds a B.A. from Fordham University, an M.A. from SUNY at Stony Brook, and a J.D. from Brooklyn Law School. He is a member of the New York State and District of Columbia bars.

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LENGTH: 1576 words

HEADLINE: SKILLED WORKERS WATCH THEIR JOBS MIGRATE OVERSEAS

BYLINE: By KEITH BRADSHER

DATELINE: WASHINGTON, Aug. 27

BODY:

Texas Instruments is designing some of its more sophisticated computer chips in India. Motorola Inc. recently set up computer-programming and equipment-design centers in China, India, Singapore, Hong Kong, Taiwan and Australia, and it is looking for a site in South America.

And while big American banks already process some account statements overseas, large accounting firms and insurance companies are looking at ways to prepare American tax returns and handle American insurance claims in East Asia.

The day may yet arrive when millions of Americans will desert their offices for laptops in exotic lands. But corporate America has already made half of that vision a reality, many economists say. It is getting a lot of work done on foreign shores -- but not by Americans. Instead, corporations are paying educated locals to do the same chores for a fraction of the cost.

The new tools of the information age were supposed to help the United States regain an edge in international competition. And while that has happened in many advanced-technology industries, the combination of powerful personal computers and high-capacity undersea telephone cables is also subjecting millions of white-collar Americans to the same global wage pressures that their blue-collar counterparts have long faced. As with steel and garment workers, the white-collar workers' positions and salaries increasingly depend on whether they can justify their higher pay with higher productivity.

The transfer of semi-skilled jobs overseas is hardly new. American companies have long assembled computer circuit boards in Malaysia, for example, and Western financial-services concerns have done processing work in Singapore.

But consulting firms say the shift is taking place at an accelerating rate and involves ever-higher-paying jobs. Constant improvements in computers and communications, particularly modems, have made it easier and cheaper to move large quantities of computer data, even for complex engineering designs. And foreign workers are designing more advanced products, like chips for complex graphic and multimedia applications.

"There's a really strong parallel to the 1960's and 1970's, when U.S.

manufacturers sent everything offshore," said Thomas G. Watrous, the managing partner of the Andersen Consulting office in Manila. "The difference is it's being done electronically."

Such moves can mean real pain for some Americans. When Sea-Land Services Inc. asked Jessie B. Lindsay, a longtime computer programmer for the company, to sign form letters to Congress last winter supporting legislation to protect American shipping jobs from foreign competition, she loyally agreed.

But a week later, Sea-Land, a unit of the CSX Corporation, announced that it was shutting down her division in Elizabeth, N.J., laying off most of the 325 employees and subcontracting the work to programmers in India and the Philippines. Mrs. Lindsay was offered a job at least temporarily in Charlotte, N.C., to make sure the transition went smoothly, but quit because she had a baby and was reluctant to move.

"I felt betrayed," Mrs. Lindsay said. Her family faced that situation twice last winter. Her husband, William F. Lindsay, also left his programming job at the American International Group when it, a large insurance company, brought programmers from India to his office and began training them to replace the American workers.

Many fear that the growing tendency of corporations to farm out tasks to developing countries is widening the gap even further between the rich and everybody else in American society by eliminating some categories of high-skill, high-wage jobs that make up the heart of the middle class. But the temptation to use cheap foreign labor is too great for companies that are desperate to stay competitive in an increasingly global marketplace.

India is fertile ground for these companies because it inherited a strong English-language school system from the days of British rule, and has emphasized mathematical education since then. Yet computer scientists trained at Indian universities come relatively cheap. Experienced programmers command salaries of $1,200 to $1,500 a month, compared with $4,000 to $6,000, or even $10,000 for stars, in the United States. The result has been explosive growth in the number of Indians working on computer programs, mainly for the American market, to nearly 75,000 today from several thousand in the early 1980's.

New jobs overseas do not necessarily mean the elimination of jobs in the United States, of course. Indeed, while Sea-Land laid off many of its programmers, Motorola and Texas Instruments are expanding in the United States as well as abroad and attribute their overseas moves in part to a scarcity of good engineers in the United States.

"Software applications are growing so quickly that we're nowhere near a finite number of jobs to be parceled out around the globe," Labor Secretary Robert B. Reich said in an interview.

Some of the best-paid computer jobs in the United States require writing original programs for a customer's precise needs, and these jobs tend to be staying, experts said.

But rapidly evolving computer technologies are turning skilled tasks into routine work that can easily be shipped overseas. Mainframe computing jobs like Mrs. Lindsay's are particularly vulnerable because many companies are changing

over to networks of desktop computers, and many Asian programmers specialize in adapting software to run on different computers.

All of this keeps the pressure on the United States to maintain its technological edge over the rest of the world.

Mr. Reich contends that many high-technology jobs will inevitably remain in the United States because electronic mail and facsimile machines are no substitute for working side by side with customers and colleagues. "It's the rubbing of shoulders, the cup of coffee over a lunch counter, where the spark of innovation occurs," he said.

Still, for many tasks, companies like Sea-Land say they must spread their work to lower-cost countries to stay competitive. "Any service like this we would shop on a worldwide basis," said M. Clint Eisenhauer, a spokesman for Sea-Land.

The exodus of white-collar jobs to developing countries troubles some economists. Even those who dismissed the warnings of politicians like Ross Perot and Patrick J. Buchanan that dismantling North American trade barriers would lead to a flight of blue-collar jobs to Mexico say the danger is all too real for skilled labor.

These economists argue that companies will often want to keep their factories in the United States to be close to good roads and railways that can supply their raw materials and deliver their goods to market. But, they add, the growing part of the economy based on ideas and information does not always need such physical proximity.

Prof. Jagdish Bhagwati of Columbia University, a critic of the notion that freer trade jeopardizes unskilled labor, for example, takes a different stance when it comes to skilled workers, particularly in the computer industry. "You're definitely seeing an enormous integration of the markets, and therefore a drag on the real wages here of the semi-skilled, of the computer programmers, of the skilled," he said.

Texas Instruments, for example, does not have to worry about infrastructure for its computer-chip-designing operation in Bangalore, India. All it needs is a private satellite link. The system works so well that the company has announced plans to expand the Bangalore office by 40 percent, to 350 workers.

Rick Younts, the executive vice president for international operations at Motorola, said it was not just lower wages that made Asian sites so attractive. Engineers in the United States can work on a project during the day, then send it electronically for more work in Asia while they sleep. As a result, projects can be completed in up to 40 percent less time, said S Remadorai, the deputy chief operating officer of Tata Consulting Services in Bombay.

Until recently, many such companies were reluctant to hire foreigners. "The arrogance that we used to have, that nobody could be as good as we were, except maybe a European, is all going away now," said Edith Holloman, the Washington representative of the American Engineering Association, a trade group based in Fort Worth.

To be sure, skilled American workers maintain many advantages over their

foreign counterparts and also benefit from the upgrading abroad through increased demand for their own output.

For now, though, the increased foreign competition has set off a political backlash in the United States. The Software Professionals' Political Action Committee, a lobbying group in Austin, Tex., wants to limit immigration visas for computer programmers. Sea-Land, American International and other companies have brought foreign workers into the United States temporarily under such visas for training, before sending them back to do their jobs in their home countries.

But the overall direction of American immigration policy in recent years has been to encourage skilled workers to come to the United States and discourage unskilled workers.

And even if policy makers wanted to, it might well be impossible to build walls around the country. Clearly, Professor Bhagwati said, American companies will go wherever they can find the best deals. "This is relentless," he said.

GRAPHIC: Graph: "Investing Abroad" shows the total value of American stakes of 10 percent or more in businesses abroad. (Source: U.S. Department of Commerce)(pg. D6)

LANGUAGE: ENGLISH

LOAD-DATE: August 28, 1995

Mexico and the NAFTA critics

By David Dreier

Mexican President Ernesto Zedillo's visit to Washington this week is sure to be greeted with another round of recycled rhetoric from protectionists claiming the North American Free Trade Agreement (NAFTA) is costing American jobs.

The usual crowd of NAFTA critics continues to cite the impact of Mexico's financial crisis as proof that NAFTA is every bit the job-killer they claimed in their unsuccessful effort to torpedo the agreement in 1993. Fortunately for U.S. workers and business, the facts tell a different story.

In NAFTA's first year, U.S.-Mexican trade surged at a record pace, from $80 billion in 1993 to $100 billion in 1994. U.S. and Mexican exports to the other's market rose more than 20 percent, or about $10 billion each. Even using the most conservative export/jobs multiplier, this created more than 100,000 U.S. jobs, adding to the 700,000 U.S. jobs already supported by trade with Mexico.

In 1995, U.S. export growth has been temporarily slowed because of Mexico's financial problems. Yet despite the peso crisis, U.S. exports to Mexico for the first half of 1995 still exceed pre-NAFTA levels. This is quite remarkable given the severe 10.5 percent drop in Mexico's second quarter 1995 GDP, and illustrates that NAFTA provides U.S. firms significant advantages over their competitors from Europe and Asia.

Rep. David Dreier, Republican of California, is chairman of the Subcommittee on Rules of the House, which has legislative jurisdiction over expedited procedures for trade agreements.

Even with the relatively good news regarding short-term export performance, it must be remembered that NAFTA is a long-term proposition. It reduces tariffs and other trade barriers over 15 years. Short-term swings in the business cycle — and certainly Mexico's current economic downturn — will cause trade figures to vary from year to year.

NAFTA's benefits are also not limited to opening a market for U.S. exports. Another goal of NAFTA is to spur business partnerships and global competitiveness among North American firms. On this, NAFTA is moving ahead briskly. Steady growth in Mexico's imports of intermediate goods — used to make finished products — is evidence of continuing expansion in U.S.-Mexican production partnerships.

It is important to note that some of the specific charges of the anti-NAFTA protectionists are simply incorrect. For examples, it is charged that all of the proposed benefits to the United States from NAFTA were lost when the value of the peso collapsed. In reality, NAFTA prevented the kind of collapse of U.S. exports to Mexico that occurred the last time the Mexican economy suffered severe trouble.

Following Mexico's 1982 debt crisis, the Mexican government essentially closed the country to imports from the United States. U.S. exports dropped 50 percent and took six years to recover. With NAFTA, Mexico is legally committed to keeping its market open to U.S. goods. By preventing a repeat of the protectionism of 1982, NAFTA protected hundreds of thousands of U.S. jobs.

NAFTA is also helping Mexico increase its exports and speed its economic recovery. A 32.1 percent jump in exports this year and a more modest 7.2 percent decline in imports is reversing Mexico's large trade deficit. As Mexico recovers, so will demand for U.S. goods and services and the more balanced trade growth that characterized NAFTA's first year.

One of the more specious claims by NAFTA critics is that Mexico's trade surplus this year could cost 340,000 U.S. jobs. They obtain this job figure by misusing the exports/jobs multiplier — which economists say generates 12,000 to 20,000 jobs for each $1 billion in new exports. It makes sense that new export production will support jobs, because those exports represent new sales for U.S. firms. However, you cannot claim the opposite — that new imports to the U.S. from a particular country displace U.S. workers — because those imports may simply take the place of imports from some third country.

The Department of Commerce has correlated U.S. trade figures with national employment numbers to show that our imports do not relate to U.S. employment. For example, from 1982 to 1987, our trade deficit quintupled, but employment rose 12.9 million and unemployment fell from 9.7 percent to 6.1 percent. From 1987 to 1991, the trade deficit was cut in half. Remarkably, employment rose again by 6.3 million, but unemployment increased to 6.7 percent. Finally, from 1991 to 1994, the trade deficit doubled, employment increased and the unemployment rate declined.

Clearly, the long-term economic impact of NAFTA will be to promote increased efficiency and private-sector job creation in the United States, Mexico and Canada. Even through the recent peso collapse, a self-inflicted economic crisis from which Mexico is already recovering, NAFTA has proven itself a win-win-win proposition.

WASHINGTON TIMES, OCT. 10, 1995

THE WALL STREET JOURNAL.

MONEY & INVESTING

THURSDAY, OCTOBER 12, 1995

INTRINSIC VALUE/By Roger Lowenstein

Will Flat Wages Beget Future Trouble?

In five years, half the people on welfare will be busy as bees, some flipping hamburgers, some grilling tunas, and some, no doubt, toiling as economists. Even better, little money will be required to train or coax these freeloaders into adapting to the blissful routine of the work week. Hence, very little funding will be available. Better still, with wages rising so fast, tax credits for the working poor—what Ronald Reagan called the best antipoverty program ever—will be unneeded.

All this may be inferred from recent actions of Washington budget-cutters. It happens that none of it is credible to economists, particularly on Wall Street.

In fact, said economists are increasingly worried about an opposite set of trends. Throughout the recovery, job growth has been anemic and downsizing has continued. Adjusting for inflation, wages have been flat for a decade. And the relative rewards for unskilled, untrained burger-flippers (and economists) have fallen.

The trends are so strong that some Wall Streeters have begun to sound like radicals. Stephen Roach, chief economist at Morgan Stanley & Co., an institution not known for harboring subversives, warns of a "backlash" unless workers "begin to receive a just reward for their productivity contributions."

Mr. Roach was among the first to predict that service industries would discover the joys of laying off workers, just as smokestack factories had. In 1991, he predicted this would lead to economic growth, corporate profit growth, lower inflation, increased U.S. competitiveness and (in case you care) rising stocks. Predicted and delivered.

His colleagues now ask, "Who could ask for more?"

Mr. Roach replies (we paraphrase), "the proletariat."

For many decades, he notes, wages rose and fell with productivity. In other words, as companies earned more for each employee, the value (and wages) of workers rose. In the 1980s, productivity began to leave wages behind. In the 1990s, the two have become totally unhinged.

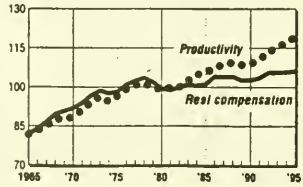
This is partly because employers are paying more for fringe items, including higher contributions to Social Security and worker's compensation. And of course, in part, it's because workers overseas demand less than employees here.

Regardless, workers have reason to feel they are missing the fun. According to Mr. Roach, while profits have boomed, the recovery has generated 6.5 million fewer jobs than a "normal" expansion. He sees "an unmistakable sign that political and social tension is going to boil over." Perhaps, in know-nothing but hard-to-resist pressures for trade barriers. Maybe, in demands for reflation. Possibly, in unions returning from their decade-long coffee break, as they have at strike-crippled Boeing Co. Failing those, anti-incumbent fervor could become permanent politics.

Economists who disagree with Mr. Roach—and there are plenty of them—still share his basic concern. Peter Bernstein, an economist of eclectic tastes, thinks workers will remain cowed, but is hardly pleased about it. A consequence of perpetually low wages would be perpetually slow growth (no raise, no new minivan). This would be bad for society, bad for the Dow Jones industrials. "The wage thing is serious," he adds. Ditto, David Shulman at Salomon Brothers.

Wages Fall Behind

Productivity vs. real compensation per hour; 1982=100



Source Morgan Stanley

David Wyss, a mainstream economist at DRI/McGraw-Hill, says the issue of how to create jobs that pay a living wage worries him, because nobody knows how to do it. Mr. Wyss, like most people since the fall of communism, liberalism and Aid to Families with Dependent Children, abhors thinking in class terms. Nonetheless, he says: "It's hard to avoid. The basic fact is that the bottom 60% are losing ground. The working poor are really caught."

On the right, Michael Tanner and Stephen Moore, of the Cato Institute, argue that entry-level wages are too low to lure workers off welfare, contributing to demand for same. Government cannot raise wages, but it can cut welfare, and it is. What will replace it is unclear.

The best hope for higher wages, Mr. Moore says, is to stimulate capital investment, which usually leads to higher pay. The more money invested in business, the more productive it is, and the more that workers are "worth." He thinks a capital-gains tax cut would help.

Mr. Roach knows that such a cut would be met with smiles in the Morgan Stanley dining room, but questions whether it's needed. He's more concerned about the falling share of national income going to workers, and thinks Washington's recent moves could make it worse.

However, the two agree that only Americans with skills will be able to command a higher wage than foreigners. To Mr. Roach, this argues for more investment in "human capital." Mr. Moore, who sees federal jobs programs and such as failures, is happy to see them go. But in their absence, he allows—and he faults both political parties—there is nothing, "no policy out there," to promote higher wages.

Editorial Page Editor: Wayne Peterson
(815) 987-1333
Rockford Register Star
Sunday, Oct. 15, 1995

Rockford Register Star
INSIGHT

OUR VIEWS

Mexico's troubles aside, stay the course on NAFTA

It is one of those quirks in economics that students of the discipline accept unblinkingly, one that leaves the rest of us scratching our heads: The loss of 40,000 jobs attributed to the North American Free Trade Agreement is not a bad thing in the long run.

It is something President Clinton was in the unenviable position of explaining to the American public last week during a visit by Mexican President Ernesto Zedillo, when the future of NAFTA was explored. Despite a sparsely populated "Repeal NAFTA" bandwagon, Clinton favors continued American support of this treaty. Such support is in the country's best interests.

This 21-month-old treaty with Mexico and Canada establishes a free trade zone that constitutes the world's largest market, with $6.5 trillion in production.

It was estimated that in 24 months, the number of U.S. jobs lost as a result of opened trade would range from 20,000 to 50,000. We likely will end that two-year period on the high end. If you are one of those left jobless, or re-employed at less money, the only number that counts is one.

The tradeoff, however, holds value for everyone.

NAFTA's initial disappointing performance is blamed largely on a deep Mexican recession, and a steep drop in that country in demand for imported goods. Neither problem was predicted when Congress embarked on the historic treaty. Nevertheless, the potential for the creation of hundreds of thousands of high-paying U.S. jobs remains realistic.

However, the best case for NAFTA has not changed: It is made by looking at what would happen without the treaty.

Job creation remains a reasonable expectation through increased trade.

Mexico likely would have entered into a similar agreement with Japan. The Mexican tariff on U.S.-made cars, for instance, would have remained high while the tariff on Japanese-made cars would have been phased out.

With the United States, unable to compete in the Mexican market, thousands more U.S. auto jobs would have been lost.

The same economic disaster would have hit other U.S. exporting industries.

Like most economic treaties, NAFTA has an escape clause Congress could exercise. Despite some early disappointments, there are no credible indications that the U.S. should cut and run.

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Statement for the Record

Western Hemisphere Subcommittee

October 25, 1995

by

Albert C. Zapanta

Executive Vice President

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Almost two years ago the U.S. Congress passed the North American Free Trade Agreement. The U.S.-Mexico Chamber of Commerce believes NAFTA has and will continue to provide a framework for expanding markets, increasing trade and growing economic opportunity. Now is an important time to reflect on the accomplishments of the tri-lateral treaty, which brought Mexico, the United States and Canada into the largest free trade area in the world. It is also time to look ahead to our relations within the hemisphere, approve fast track negotiating authority for the nation's Executive office and cement relations with emerging markets in the region.

One important, and largely expected result of NAFTA: trade flows have increased dramatically between the North American trading partners. Through the first six months of 1995, the United States has sent more goods to Mexico, and Mexico has sent more goods to the United States, than during the same period in any pre-NAFTA year. While this year there has

* The United States-Mexico Chamber of Commerce, incorporated in 1973 in the District of Columbia as a 501 (C) (6) non-profit corporation is a chartered, bi-national chamber promoting trade and investment between the two American nations. The Chamber represents nearly 1,000 businesses and maintains offices in Washington, DC, Los Angeles, Dallas, Tampa, Chicago, New York, Denver, Seattle, Mexico City and Monterrey, Mexico.

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been a drop-off in U.S. exports to Mexico compared to 1994, they are still above 1993 -- or any previous year's -- level. According to the U.S. Department of Commerce, the U.S. shipped $25.9 billion in goods to Mexico from January to June, 1995, compared with $23.6 billion in 1992, $24.2 billion in 1993 and $28.6 billion in 1994 (figures are not seasonally adjusted). This equates to an increase of $1.7 billion, more than 7 percent, in U.S. exports to Mexico between 1993 and 1995. Meanwhile, overall trade flows between the months of January and August have gone from $64.34 billion in 1994 to $72.95 billion in 1995.

Mexico, meanwhile, exported $34.9 billion in commodities to the United States in the first six months of the year, a nearly 29 percent increase over the previous year, according to the DOC. Some critics point to a U.S. trade deficit with Mexico as a weak point of NAFTA. That view oversimplifies the relationship between the United States and Mexico. United States-produced intermediate goods feed the growing maquiladora industry, intra-industry trade is an important and often overlooked aspect of U.S.-Mexico commerce, and foreign direct investment has steadily increased through the past several years. Between 1993 and 1994, Mexico's FDI in the United States jumped from $1.21 billion to $2.19 billion, with the largest increase in the manufacturing sector, according to the U.S. Department of Commerce. U.S. investment in Mexico jumped from $15.22 billion to $16.38 billion.

Clearly, ties between the nations are becoming stronger. Common economic interests are leading the nations toward a healthier, integrated market. In addition, one goal of the treaty -- the competitive position of the three NAFTA nations compared to the rest of the world -- is often overlooked. National leaders established the treaty to enhance the competitiveness of North America relative to the European Union, the Pacific Rim and other markets. It was not set up so

U.S. or Mexican analysts could dissect the current accounts of the countries and pronounce victories and defeats based on each dollar or peso, each good or service, crossing the border.

More time is needed before a final analysis of NAFTA and its impact on competitiveness is ready. But already we see that NAFTA has provided for increased trade, which means increased production, in each nation.

In addition, NAFTA worked as a calming influence during Mexico's economic crisis, helped the United States and Mexico agree on a support package for the peso following the devaluation, and is helping the nations prepare for more open trade in the hemisphere. NAFTA itself was unrelated to Mexico's economic crisis. The nation's government failed to foresee the results of serious macroeconomic imbalances. NAFTA does not regulate macroeconomic controls, and is completely unobtrusive to national policy in this matter. Also, Mexico suffered through political difficulties when there was an uprising in Chiapas on January 1, an assassination of a presidential candidate, a series of kidnappings, a hotly contested election campaign, the murder of a political leader in Mexico City, and a number of scandals linking drugs, politicians and police. Each of these events, completely unrelated to trade or NAFTA, led to a withdrawal of capital from Mexico's foreign exchange reserves, pushing along the eventual devaluation and crisis. The implementation of NAFTA, however, caused the shocks throughout North America to be less severe. In the past, Mexico has turned inward during economic crises, raised import barriers and closed itself to foreign goods. This did not happen in 1995. Instead, Mexico continued to implement NAFTA provisions, and continued to receive U.S. exports.

On another front, the treaty has provided a framework for settling trade disputes. Within the framework of NAFTA, the U.S. Department of Agriculture lifted some quotas against

Mexican fresh vegetable growers; a panel limited countervailing duties against leather clothing from the United States -- and are ordering U.S. Customs to pay back $400,000 in taxes to Mexican companies -- and steel-exporting companies from the U.S. won a boost when a panel found unfair restrictions on hot-rolled steel plate.

Individually, the cases are important to specific firms. Overall, they are important to free trade, economic growth and economic competitiveness. This growth and competitiveness link to the security of Mexico and the United States. The best social program available in any country is a good job. If the U.S. Congress wants to stop illegal immigration and drug trafficking, it must consider the positive impact the U.S. economy, the largest in the world, can have on our neighbors to the south.

NAFTA has proven itself both strong and flexible in the face of economic crisis and offers the groundwork for economic growth in coming years. Now is not time to hold back. Now is time to move forward with trade agreements and time to begin incorporating Chile and other nations in the hemisphere. Fast track authority is imperative to the negotiating process. We are at an important juncture in our relations with Latin America, and the direction we choose will determine the strength of U.S. leadership in the hemisphere for many decades. Our path is clear: we must move ahead with plans to create the largest and most prosperous trade block in the world.

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